March 1957

THE CANADIAN CHARTERED ACCOUNTANT

THE CANADIAN INSTITUTE OF CHARTERED ACCOUNTANTS

CANADA'S ECONOMIC PROSPECTS

A review of Royal Commission Report
25 year projection of population, industry and trade

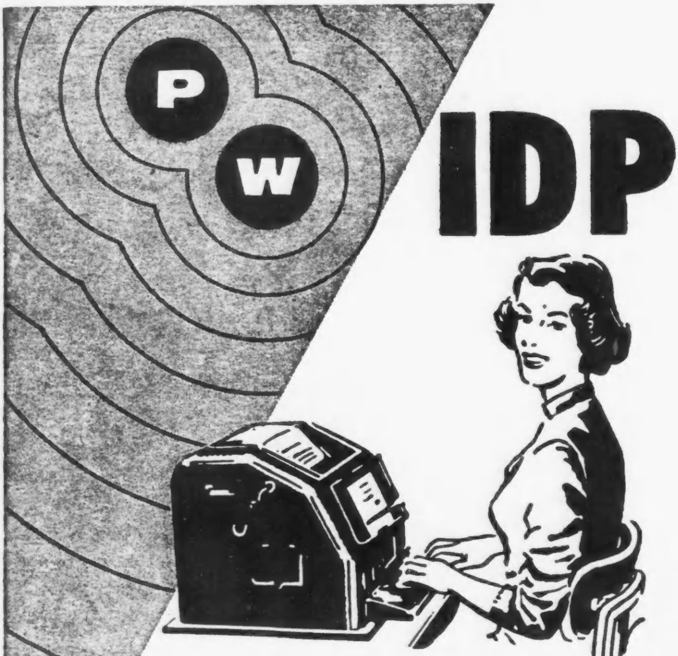
Internal Control and the Audit

The Business of Canada's Defence Spending

Preparing Tax Returns by Diazo-Type Process

I.D.P.—A Case History

PRACTITIONERS FORUM: Processing Tax Returns
ACCOUNTING RESEARCH: The Standard Bank Confirmation Form
TAX REVIEW: Instalment Sales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THE CANADIAN

CHARTERED ACCOUNTANT

VOL. 70, NO. 3, MARCH 1957

Opinions expressed are not necessarily endorsed by The Canadian Institute of Chartered Accountants

Published Monthly by

THE CANADIAN INSTITUTE OF CHARTERED ACCOUNTANTS
69 Bloor Street East, Toronto

The editor invites members and others to submit articles for publication
Manuscripts should be typewritten and double-spaced.

Subscription Rate $6.00 per Year; *Single Copies*: Current and five immediately preceding volumes — 60c; earlier volumes — $1.00

Printed by General Printers Limited and mailed at Oshawa, Ontario
Authorized as second class mail by the Post Office Department, Ottawa

IN THIS ISSUE

W. A. MACKINTOSH

With the recent publication of the preliminary report of the Gordon Commission on Canada's Economic Prospects, interest in Canada's long range economic position takes on new meaning. The 60,000 word public document presents a remarkably clear analysis of our future in terms of population, production, wages and so on and, providing our destiny does not lead us along the road to war or depression, the picture which the Commission has drawn is, on the whole, exhilarating and attractive. It does not, however, hide the fact that with our rapid growth there are also serious problems.

It was suggested that Dr. William A. Mackintosh might be persuaded to present our readers with *A Review of the Preliminary Report* and fortunately the editor was successful in obtaining this article for *The Canadian Chartered Accountant.* The author draws his observations from long and close association with both economic and social forces.

Dr. Mackintosh is principal and vice-chancellor of Queen's University, Kingston and has been a leader in the field of economics as lecturer, author and member of many committees and societies over the past 40 years. He has authored and co-authored a notable list of studies such as "Economic Problems of Prairie Provinces", "Statistical Contributions to Canadian Economic History" and "Economic Background of Dominion-Provincial Relations". From 1939 to 1946 he held advisory posts in the Federal Departments of Finance and Reconstruction and during this period served as Acting Deputy Minister of Finance. For his work he was created a Commander of the Order of St. Michael and St. George. Dr. Mackintosh received his doctoral degree in philosophy in 1922 from Harvard University. In recent years several Canadian universities have bestowed honorary degrees upon him for his distinguished services.

W. E. SHIELDS, C.A.

Audit procedures have changed during recent years to meet the constantly increasing demands of business and reliance is being placed more and more upon the system of internal control in determining the scope of the audit. In "The Review of Internal Control and the Audit Program" W. E. Shields takes a look at the steps which are necessary for the review of the system of internal control in order to facilitate the audit program work. He examines the amount of procedure testing that needs to be done, considers its timing and discusses the way in which the review should be presented before the audit can be carried out. Mr. Shields is a partner of Clarkson, Gordon & Co., Winnipeg, and obtained his certificate in chartered accountancy in 1953. He is a member of the Institutes of Chartered Accountants of Manitoba and Ontario.

GEORGE F. WEVILL, C.A.

Canada's defence program has been and will probably remain in the top headlines for many years. World conditions have made it necessary to develop a production potential which can keep abreast of the changing needs of the defence services and

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also expand rapidly at short notice. Buying experience over the years has demonstrated the value of centralized procurement and in "The Business of Canada's Defence Spending" George Wevill draws on a wealth of experience to explain in broad terms the services involved in the purchasing of stores, equipment and construction by the Department of Defence Production currently totalling over $1,-000,000 a year.

After spending the early part of his life as a member of the profession in Japan and Korea, Mr. Wevill practised for a brief time with Clarkson, Gordon & Co., Toronto and in 1943 served as controller of accounts of the Inspection Board of the United Kingdom and Canada. Since 1946 he has been comptroller of Canadian Commercial Corporation and in 1951 he assumed the position of comptroller of the Department of Defence Production. He is a Fellow of the Institute of Chartered Accountants in England and Wales and a member of the Institute of Chartered Accountants of Ontario.

CHARLES F. GAVILLER, C.A.

Increasing the speed and accuracy of filling out tax returns is a matter of continual interest to accountants. Accounting firms across the country have studied this problem for a number of years and in "Preparing Tax Returns by the Diazo-type Process", Charles Gaviller has come up with a solution which is meeting his company's particular requirements. Tax returns can be reproduced by several types of equipment and various methods are being used to eliminate the typing bottleneck. A comprehensive review will be published in *The Canadian Chartered Accountant* at a subsequent date.

Mr. Gaviller, a partner in the firm of Gaviller, McIntosh & Ward, Owen Sound, Ontario, has been a member of the Institute of Chartered Accountants of Ontario since 1947.

A. A. MACKEY

The management of any large company has an obvious interest in increasing the effectiveness of its clerical and accounting operations. A thorough analysis of what has been accomplished by the Canadian National Railways in order to provide more useful statistical and control information at lower cost is provided by Arthur Mackey in "Integrated Data Processing – a Case History". A payroll conversion program covering 117,000 employees from a manual to a tabulating method may well be considered as among the most difficult of its type yet carried out in Canada. Mr. Mackey's article not only covers the planning and implementation processes but deals with some of the lessons which were learned during the completely successful changeover.

Mr. Mackey has been with the Canadian National Railways since 1954 and is currently Supervisor of Machine Accounting Methods. Prior to World War II, he had considerable experience in methods work. After the war he was associated with the electrical manufacturing industry where he was engaged in the application of punched card and electronic accounting equipment to accounting and plant control procedures.

EDITORIAL

The subject of this month's editorial is the position of the auditors at company meetings. T. A. M. Hutchison writes that, while the auditor may

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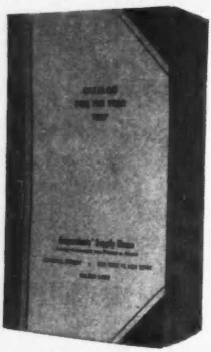

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have the right to attend meetings of shareholders, there is little indication that he has, in practice, availed himself of this privilege. On the other hand, Mr. Hutchison points out that when an auditor does attend a meeting, it is essential for him to have a clear understanding of his position. His commentary should be of great interest to auditors of companies who, under the Dominion Companies Act, are entitled to attend any meeting of shareholders.

Mr. Hutchison is senior partner of Peat, Marwick, Mitchell & Co., Toronto, and a former chairman of the Board of Governors, Canadian Tax Foundation. Since 1952 he has acted as treasurer of the Canadian Institute of Chartered Accountants. He has wide experience on matters relating to the Canadian Companies Act, the Ontario Corporations Act and the Ontario Securities Act, having served as chairman on a committee to deal with the Ontario Corporations Act and as a member of the Canadian Institute's committee on the Canadian Companies Act. He has recently been appointed a member of the Canadian Institute's Committee on Accounting and Auditing Research.

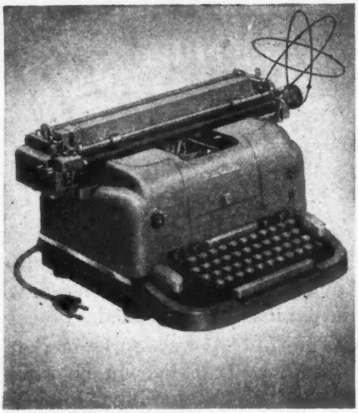
FORTHCOMING FEATURES

HOW THE FEDERAL TAX DEPARTMENT OPERATES
H. F. Herbert

CASH FORECASTING
A. F. D. Campbell

FINANCIAL CONTROL OF ONTARIO MUNICIPALITIES
Paul Hickey

CAPITAL FOR SMALL BUSINESS
W. S. Hulton



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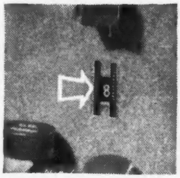

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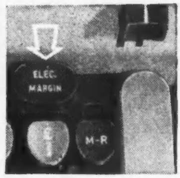

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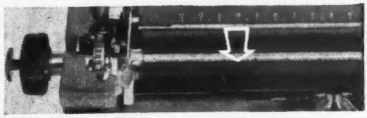

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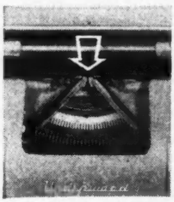

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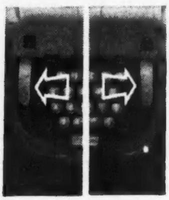

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NOTES AND COMMENTS

"Fighting Words"

On March 3, the Canadian Broadcasting Corporation's weekly T.V. panel show "Fighting Words", will discuss the subject of taxes. Two chartered accountants have been chosen to participate on the four man panel. The program will be carried "live" in the Toronto and Montreal areas. It will also be seen throughout the country within a week or two after the "live" showing, depending on the locality.

Now 7,000 C.A.'s in Canada

At January 31, 1957 the number of chartered accountants in Canada passed the 7,000 mark. At present the total is 7079 and is expected to reach 7,300 before the year is over.

Income Tax Recommendations

More generous exemptions for married persons and an easing of the restrictions governing allowances for medical expenses were included in the proposals for income tax changes submitted by a joint committee of the Canadian Institute of Chartered Accountants and the Canadian Bar Association to the Ministers of Finance and National Revenue. The brief also repeated its request of last year that all bona fide business expenses should be allowed in computing income for taxation purposes, and suggested that charitable donations in excess of 5% of a corporation's income or 10% of an individual's income made in any year should be deductible in any of the five succeeding years when the limit is not exceeded.

The C.I.C.A. was represented at the meeting by L. C. Frewin, chairman of the Taxation Committee, John Kinghorn, Harold Crate and E. M. Howarth, executive secretary of the Canadian Institute. Bredin Stapells and E. B. Fairbanks were spokesmen for the Canadian Bar Association.

Club Fees Allowable Deductions

Social and service club fees paid by the Royal Trust Company on behalf of its senior officers are deductible from income tax, according to a judgment handed down in the Exchequer Court by Mr. Justice Thorson. In 1952 the company paid for 78 memberships in 48 clubs and claimed it had obtained many valuable investments as a result of the contacts these memberships produced. In Mr. Justice Thorson's view, its action was in accord with good business practice and the fees paid were allowable business expenses. His ruling reverses a decision of the Income Tax Appeal Board.

Taxpayer v. MNR

In 1956 the taxpayer kept the Courts and the Income Tax Appeal Board very active, according to a report made by CCH Canadian Ltd. Of 184 Board decisions, 79 favoured the Taxpayer and 105 the Minister of National Revenue. The Minister took

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Index to Modern Figuring by Marchant Methods . . . . . . ☐

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four appeals to the Exchequer Court and won them all; the taxpayer took ten appeals to this Court and won five. The Supreme Court heard two appeals by the Minister and found in his favour in both cases.

Cost of Gordon Report

The work of the Gordon Royal Commission on Canada's Economic Prospects has cost the government $1,235,500 so far and will require another $150,000 in the next fiscal year to complete the final report.

Study Ten Years of Confederation

A Royal Commission to inquire into the effects of Confederation on the economic life of Newfoundland will be set up this year. When Newfoundland became Canada's tenth province in 1948, the terms of agreement included a provision for this commission.

Sales Tax Manual

A new handbook dealing with sales tax and other excise taxes has been published by the Canadian Manufacturers Association. It supersedes the 1950 edition and contains 450 pages of up-to-date information designed to assist manufacturers, purchasing agents, accountants and lawyers. Copies may be obtained from the Canadian Manufacturers Association, 67 Yonge St., Toronto, at $10 each.

Bahamas Trust Company

A new development in international financial cooperation appears in the formation of Bahamas International Trust Co. Ltd. in Nassau, Bahamas. Although this trust company has been incorporated in the Bahamas and is managed and controlled in that country, it owes its existence to a group of financial houses on both sides of the Atlantic. The company is sponsored by Barclays Bank D.C.O., Hambros Bank Ltd., Robert Fleming & Co.

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On the steps of the Parliament Buildings, Ottawa when a joint committee of the Canadian Institute of Chartered Accountants and the Canadian Bar Association presented submissions dealing with taxation matters. Left to right: H. E. Crate, F.C.A., R. B. Stapells, L. C. Frewin, C.A., M. G. Teed, Q.C., E. B. Fairbanks, J. P. Kinghorn, C.A. and E. M. Howarth.

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Ltd., The Royal Trust Co. of Canada, London, and the Anglo-American Corp. of South Africa Ltd., and, from this side of the Atlantic, by the Empire Trust Co., New York, The Royal Trust Co., Montreal and E. D. Sassoon Banking Co. Ltd., Nassau.

Bahamas International Trust Co. Ltd. has an authorized capital of £1,000,000 of which £200,000 has been issued and paid up at a premium of 50% giving present total capital funds of £300,000. The company is to conduct a financial, trusteeship and general investment business.

AIA Research Bulletin

"Business Combinations" is the subject of Accounting Research Bulletin No. 48 issued in January by the Committee on Accounting Procedures of the American Institute of Accountants. This bulletin deals with the accounting treatment appropriate to two types of business combinations—*purchases,* in which the former ownership is eliminated, and *pooling of interests,* in which substantially all of the ownership is continued.

Australian Research Foundation

An Australian Chartered Accountants' Research and Service Foundation has been licensed as a company to act as a research and service organization for the Institute of Chartered Accountants of Australia. Professor Mary E. Murphy, Ph.D. (Lond.), C.P.A. has been appointed its research and service officer.

Electronics Explained

A new 40-page booklet published by the National Office Management Association takes the mystery out of electronics in office automation. Titled "Appraisal of Electronic Business Applications", it explains in nontechnical language the basic differences between mechanical and electro-mechanical machines and provides a yardstick for evaluating the utility and cost of automation for various office procedures. Copies of the book are available at $2.00 each from the Association, 132 W. Chelten Ave., Philadelphia 44, Pa.

Accountants' Magazine, Diamond Jubilee

The journal of the Institute of Chartered Accountants of Scotland, *The Accountants' Magazine*, celebrated its 60th anniversary with the January issue. To the present editor, E. H. V. McDougall, and *The Accountants' Magazine* we wish continued success in the years to come.

In the News

Harry O. Patriquin, a member of the Alberta Institute, has been appointed a director of the Bank of Canada.

Another member of the Alberta Institute, Walter Nobbs, has been appointed a member of the Board of Public Utility Commissioners under an order in council recently passed by the Alberta Government.

Imperial Bank of Canada has appointed George M. Black, Jr., of the Manitoba Institute, to its board of directors.

James M. Dunwoody has been elected a director of the Mercantile Bank of Canada.

Serve by Giving

When there is a need for help, your Canadian Red Cross serves across the street, across the nation and across the world.

Editorial

AUDITORS AT COMPANY MEETINGS

THE REFERENCE to auditors attending at company meetings is, of course, directed to meetings of shareholders because auditors, in their capacity as auditors and as financial consultants and advisors, frequently attend company meetings of directors and executives. In Canada, as in the United Kingdom and in most parts of the British Commonwealth, auditors are normally appointed by the shareholders at the annual meeting. This is not the case in the United States where in the majority of cases the appointment of "independent accountants", as they would be called in that country, generally is made by the directors or management.

The Dominion Companies Act, which became law in 1934, provides that the auditors of a company are entitled to attend any meeting of shareholders at which accounts examined by them are to be submitted to the shareholders. The British Companies Act of 1948 provides that the auditor shall be entitled to attend any meeting of shareholders and to receive all notices of such meetings and to be heard at any such meeting on any part of the business of the meeting which concerns him as auditor. When the special committee on the Dominion Companies Act was appointed by the Canadian Institute of Chartered Accountants in 1951, consideration was given to this matter and a recommendation made to adopt a provision similar to that contained in the British Companies Act. The Province of Ontario, in enacting its new Corporations Act in 1953, accepted this recommendation. It is obvious, therefore, that in Canada the profession considers that the auditor should be entitled to attend any meetings of shareholders of a company and to express his views on any matter which concerns him as an auditor of the company.

While the auditor may have the right to attend meetings of shareholders, there is relatively little indication that in practice, he has availed himself of this privilege. Many auditors probably have one or two clients who make a special point of inviting them to attend annual meetings of shareholders, but in most instances the invitation will be issued mainly as a courtesy and not for the purpose of enabling the stockholders to seek information from the auditor. Auditors appointed under the Ontario Corporations Act will, of course, receive formal notice of all meetings. With the increasing size of business enterprises, the auditor has less and less contact with the shareholders and in many cases even with the directors. Often his sole contact rests with the executive group managing the business concern. Under these circumstances there is a worthwhile opportunity when attending the annual meeting for him to meet directors, who are not officers of the company but frequently are important shareholders. While shareholders too often do not evidence sufficient interest to turn up at annual meetings, the auditor may meet those attending. He also has a chance to hear reports to stockholders by senior officers of the company and sometimes questions and comments by shareholders, all of which may help to widen his knowledge of the background of the company involved.

When the recommendation was made that the auditor should be able to be heard at any meeting of shareholders on any part of the business which concerns him as auditor, it was obviously intended to provide him with an opportunity to explain matters or give information to shareholders on particular situations where he felt that the financial information should be amplified. While there may be occasions when he feels it necessary to present his viewpoint orally at a meeting, generally speaking he would be well-advised to see that the financial statements present the information required in proper form and that his formal report thereon clearly sets out his views. Normally the auditor would attend a meeting as an observer. If he is questioned or asked to provide information on any matter, a difficult problem may arise for him. Questions of shareholders would be handled by the chairman of the meeting and the auditor before replying would need to know that the chairman considered the question in order. While he can provide such information as the chairman or the meeting considers to be in order, the auditor must be very careful not to offer to shareholders without approval of the meeting, information which management considers should be kept confidential. This is not to suggest that shareholders are not entitled to all the information needed to make a fair presentation of the financial affairs of a company, but the place for the auditor to see that this is done is in the financial statements and not at the annual meeting. It is therefore essential that when an auditor attends a meeting of shareholders, he has a clear understanding of his position.

The Business of Canada's Defence Spending

G. F. WEVILL

CANADA, since 1939, has adhered to the principle whereby the placing of contracts for supply of the goods and services required by her armed forces is the responsibility of civilian government purchasing agencies acting independently of the Department of National Defence.

Buying experience over the years has demonstrated the value of centralized procurement. In addition, there is need for control over the allocation of the productive resources of the nation required for defence production, with due regard for the just demands from all sectors of the economy. During the Second World War, this centralized job was in the hands of the Department of Munitions and Supply. Today the work is carried out by the Department of Defence Production and by Defence Construction (1951) Limited. Only in such limited fields as the construction of married quarters and schools for armed forces' personnel or the building of airfields are other Canadian Government procurement agencies involved.

During the past five years National Defence has expended $8¾ billion, broadly divided into two classes:

(a) $3½ billion for pay, allowances, and operations, and

(b) $5¼ billion for stores, services and construction.

This article will deal in general terms with the stores, services and construction portion and the action of National Defence and its aforementioned purchasing agencies, Defence Production and Defence Construction, which leads to the spending concerned. To provide some detail as to the nature of the stores, etc. involved, the expenditure planned for the fiscal year 1956-7 is as follows:

	($000)
Barrack and other stores, including uniforms	$ 55,246
Gasoline, oil and lubricants	41,847
Equipment repairs and spare parts	156,055
Property and building maintenance	62,938
Aircraft and engines	229,699
Ammunition	70,172
Ships	60,000
Electronics (excl. Mid-Can.)	44,789
Armament	29,067
Vehicles	23,513
Tanks and armored fighting vehicles	590
Other	74,758
Construction of barracks, married quarters, schools, airdromes, etc.	145,931
Infrastructure and Nato contributions	17,897
Mid-Canada Line	100,000
	$1,112,502

From any angle, this is big business, and the funds needed to handle it come mainly from the annual estimates as approved by Parliament.

There are two other sources of expendable funds, perhaps relatively minor in amount, namely:

(a) proceeds of cash from approved sales of existing defence supplies to foreign governments; and

(b) cost of existing National Defence supplies transferred as part of Canada's contribution to Infrastructure (SHAPE) and Nato countries.

Costs under (b) are charged to the specific Nato estimates and credited to the main defence spending vote, as transfers take place. The materials, in either case, will have been acquired out of prior years' defence estimates but the respending of the resulting credits calls for additional purchasing in the year of their replacement.

The Department of Defence Production (known as DDP) assists in the estimates by providing the Department of National Defence (DND), when requested, with a forecast of spending in the ensuing budget year under active contracts as well as on projects not yet under contract.

It is interesting to note that National Defence is authorized by Parliament to make commitments in any one year having a total cost substantially greater than the cash made available by the estimates. For example, the 1956-57 estimates mention a committable total of $3,470,-423,000, but the taxpayers are called on to provide expendable cash to a total of $1,722,797,000. The balance of approximately $1,750,000,-000 is noted as payable in future years. This arrangement recognizes the fact that modern defensive equipment whether for sea, land or air, by its highly technical nature, may involve long-term contracts of substantial value. Uncompleted commitments of the previous year naturally receive priority by way of charge against the new year's funds.

Role of DND in Procurement

National Defence is responsible for determining the requirements of the three Services and of Defence Research Board, drawing up the specifications and advising when deliveries are needed. To accomplish this, insofar as supplies and equipment of more common types are concerned, inventories are maintained at both central and local levels.

When the stock of any item must be replenished, a new item ordered, or a project undertaken, a formal request to purchase, usually in the form of a contract demand, is drawn up. This document, addressed to the Department of Defence Production (or to Defence Construction Limited), carries a brief but complete description of the requirement, time and place of delivery, and is signed by or on behalf of the Minister of National Defence and by the Chief Treasury Officer. The latter certifies, on behalf of the Comptroller of the Treasury, to the availability and earmarking of funds estimated to cover the proposed expenditure.

The specific approval of Treasury Board may be required before the issue of certain contract demands. These include construction projects, and those covering procurement of technical equipment in new development fields which can involve heavy cost.

This is a very brief description of an intricate procedure within National Defence which ensures full and careful consideration of all service requirements before purchasing action is requested. Because of the never ceasing advance of science and technology, months of planning, designing and redesigning may precede the issuance of a contract demand. Quantities must be determined and delivery dates and consignment points set in accordance with scheduled needs.

Important agencies in the evolution of modern processes and equipment are: (a) Defence Research Board, and (b) the Directorates of Development, under the Quartermaster General, such as Armament, Engineering, Electrical and Communications, Interservice (uniforms, etc.), and Vehicles. Investigations frequently include consultations with Allied Powers using identical or similar equipment and with Defence Production to obtain information as to the availability, cost and time required to produce, purchase or construct a specific requirement.

To keep purchasing within the bounds of approved Estimates, on the staff of each of the Armed Services, Defence Research Board, and Nato or Mutual Aid there is a financial or budget control officer. This officer maintains a record of the funds available, analyzed by main spending classes known in Government financial circles as "Primaries".

With the total estimated costs shown on each contract demand, the "primary" funds are recorded as "encumbered". Against these encumbrances are logged the cost shown by individual contracts, copies of which reach the budget control officer from Defence Production or Defence Construction.

Disbursements to defence suppliers under National Defence contracts are under the strict control of Chief Treasury Officers attached to National Defence and Defence Construction, to whom claims for payment are sent directly. Records maintained by these officers on the availability of funds range from broad classifications down to individual supplier contracts. No cheque is issued unless the related claim is fully documented, receipt of goods or services is acknowledged, and adequate money is available for the project concerned.

Each month the National Defence Treasury Officer submits to the Deputy Minister of National Defence a detailed statement of total estimates, encumbrances, and cash spending. This information is merged with the control records maintained by the financial officers of National Defence, and used to relate committing and spending to the plans and projects backing up the year's estimates.

Role of DDP in Procurement

Determining the source of supply, purchasing the needed equipment and stores, contracting for needed services, and thereafter ensuring delivery according to schedule are the responsibilities of the Department of Defence Production and represent in variety, volume and value the major element of defence spending.

The Department of Defence Production takes purchase action in response to either contract demands or service requisitions. The latter usually cover stores, materials or services of small dollar value required immediately by district establishments of the Army, Navy and Air Force. They

are issued under authority vested in senior officers of the Services located in field establishments. Such a requisition is usually sent for direct purchase action to one of the fourteen district purchasing offices of the Department of Defence Production.

A contract demand goes to the appropriate Defence Production branch according to the nature of the stores or services required. A list of these branches and of their more important sub-divisions follows:

1. Aircraft Branch
   (airframes, repair and overhaul, engines)
2. Ammunition Branch
3. Electronics Branch
   (radar and asdic, communications, components)
4. General Purchasing Branch
   (clothing and textiles, hardware, tools, electrical equipment, wire and cable, medical supplies, metals, fuel, kitchen and messing equipment, motor vehicles)
5. Gun Branch
6. Machine Tool Branch
7. Shipbuilding Branch.

The first task of the branch or buying group concerned is to determine the area of supply, and the chief point at which this information is available is the very complete and up-to-date supplier or source lists, maintained by the Secretary's Branch. Added to the information available from the supplier lists, each member of the buying group uses his specialized knowledge of industry, both domestic and foreign, in seeking the best available supply sources.

Requirements to be met from the U.S. Government, U.K. or European sources are passed for procurement action to Defence Production Offices in Washington, U.S.A., or London, England.

The majority of Defence Production contracts are awarded at a fixed price and as the result of competitive tenders. However, in selecting the successful bidder, factors other than price have to be considered, such as ability to produce to specifications and on time, performance on any previous contracts, and a sound financial condition.

The confidential nature of the tendering process, and the importance of time deadlines etc. which it involves, demands specialized attention from Defence Production, both in Ottawa and the district offices. In addition, where repair, maintenance and catering contracts at district office level are concerned, there must be careful accounting of the security deposits which accompany the bids.

The tender system is not appropriate where there is only one source of supply, or where the requirement has not been produced before. In such cases, prices are set by direct negotiation, or on the basis of actual approved cost plus an agreed fee or allowance for profit.

When the supplier has been selected, the Department drafts a covering contract. This contract will set out the quantities to be supplied, prescribe specifications, delivery dates and consignment points, such inspection as must be met before delivery will be accepted, instructions regarding packaging and preservation, prices and terms of payment, etc. As a result of years of buying experience, a series of standard or general conditions have been formulated to govern all defence contracts. These general conditions cover such matters as assignment and sub-letting, con-

duct of the work, patent and royalty claims, secrecy and protection, and use of Canadian labour.

If the value of a proposed contract is less than $10,000, the contract may be entered into immediately. If, however, it exceeds this amount, a brief but complete statement regarding the intended contract is prepared and forwarded to the Financial Adviser's Branch for review of the proposed terms. If the proposed expenditure does not exceed $25,000 (or $50,000 if the lowest tender is accepted), the contract may now be entered into by an officer of the Department acting on behalf of the Minister. Contracts exceeding these values must, except under urgent circumstances, be approved by Treasury Board to whom the proposals are passed in the form of "submissions" in which all cogent points are briefly set out.

In addition to direct purchasing, the Department of Defence Production assists the defence effort directly or indirectly by the operation of its revolving fund; by the acquisition, disposal and control of Crown-owned special production tooling, plant and equipment in the hands of defence contractors; and by the recording and administration of working capital advances to, and investments in, certain Crown companies.

The revolving fund has a maximum authorized net working capital of $150,000,000, of which there is currently utilized some $57,000,000 spread over eight main programs, from strategic stockpiles to shipbuilding components. Current assets include $35,000,000 in physical inventories, of which fabrics to a value of $17,000,000 are carried in the cloth warehouse operated by the Department. Revolving fund sales have an average annual value to date of $69 million, though currently these are running at about half that sum.

Control of the varied Defence Production transactions is maintained by means of accounting records modeled on commercial lines, from which monthly statements of account for the Deputy Minister are prepared. As of each March 31, the statement of operations and balance sheet, duly certified and reported upon by the Auditor General, form part of the Minister's annual report as laid before Parliament.

Role of DCL in Procurement

During the past five years expenditures by Defence Construction (1951) Limited on behalf of the Department of National Defence has totalled some $644 million. This organization prepares estimates, places contracts and supervises to conclusion the resultant construction work, both in Canada and in Europe, the latter activity arising from our Nato commitments. Offices are maintained in all important areas throughout Canada and there is also one in Europe.

Defence Construction is responsible for all military structures such as barracks, warehouses and hangars. Notable projects include the construction work on Mid-Canada Line and the establishment of Camp Gagetown, N.B.—which involved clearing of 40,000 acres and erection of 100 buildings exclusive of housing units.

Such procurement is based on requests equivalent to the contract demands issued to Defence Production. Each bears a certificate of the funds which will be available to the procurement agency to meet approved financial claims.

In accordance with construction practice, the system of inviting tenders by public advertisement as a rule applies. Defence Construction handles all tenders at its Ottawa headquarters. Public competitive tenders are not applicable to secret projects, or those where the isolated and remote location of the work make it impossible to establish reasonable firm prices. Contracts in such cases are based on negotiation.

When costs have been determined either by tender call or by direct negotiation, contracts may be entered into without prior approval of Treasury Board provided their individual value does not exceed $50,000 (if the lowest tender is accepted), or $25,000 where tenders are not involved. As in the case of Defence Production purchasing, such contracts must be reported to Treasury Board monthly. Proposed contracts of a value in excess of the above sums are subject to prior approval of Treasury Board.

Construction proceeds under the supervision of district and field representatives of the construction agency. On the basis of reports from these field representatives, periodic progress claims from the contractors are approved for payment. From the technical angle, completion of a construction project takes the form of a "handing over" by the construction agency and the contractor to representatives of the Defence Service concerned, all of whom sign and exchange an acknowledgment of receipt.

However, contracts not based on tendered or negotiated fixed prices, and thus subject to continuous audit in the field by Cost Inspection and Audit Division of Treasury, are from the financial standpoint not concluded until the final and accepted audited cost is reported.

Aids to Industry for Defence Purposes

World conditions, pointed up by the Korean situation in 1951, have made it necessary to develop a production potential which can keep abreast of the changing needs of the Defence Services and can also be expanded rapidly at short notice. Canada's policy is to encourage industry to undertake the job of expansion, in some cases with the added incentive of accelerated depreciation allowances. Establishment of the conditions of such allowances and control of the costs claimed are the concern of both the Department of Defence Production and the Cost Inspection and Audit Division of the Comptroller of the Treasury.

To a greater extent, however, such government encouragement has, in the past, taken the form of direct investment in plant and equipment, where facilities, needed to meet defence requirements, would be far in excess of commercial demands.

Determination of these plant requirements, their acquisition and a continuous detailed accounting for them are tasks which concern such Defence Production groups as the Financial Adviser's Branch, the Machine Tool Branch, and the Comptroller's Branch. The comptroller is responsible for physically inspecting and identifying each such item and for maintaining up-to-date inventory records showing their location, quantity, and value.

Gross outlay on these Crown-owned assets since 1951 reached a total of $156 million, but as a result of sales to user-contractors the current re-

corded total is some $60 million. The majority of these sales have been on the basis of a down payment with interest-bearing annual instalments and, although few in number, are substantial in value. In the larger transactions, the buyer binds himself, by the contract, to maintain the original asset group complete for a stated period of years; thus the defence production potential of the nation is unimpaired despite sale of the assets concerned.

As a result of this policy of expanding facilities, our defence procurement expenditures from sources outside Canada have, during the past five years, fallen from 18.5% to 3.5% of the total annual commitment.

Some Controls over Defence Contractors

Spending controls with respect to quality of all items of standard production types are exercised by Inspection Services, a National Defence organization of 2,000 persons. Lengthy and highly technical production projects, such as concern aircraft and engines, ships and weapons, are subject to continuous progress control by Defence Production representatives, and quality control by Service personnel, posted to the plants of the contractors concerned. Signed documents of approval from these representatives must support requests for payment of contractors' invoices or claims on the subject contracts.

Contracts entered into on the basis of cost plus an agreed scale of profit are subject to an audit of costs by the Cost Inspection and Audit Division of the Comptroller of the Treasury. This right of audit may by mutual consent be extended to related subtracts. It is probably well known to accountants in public practice that establishment of mutually acceptable elements of cost (while based primarily on the schedule known as "DDP 31") sometimes involves lengthy discussions on the part of skilled personnel of the contractor and his auditors on one side, and the Crown's cost auditors, financial advisers and contracting officers on the other.

Conclusion

The importance of Canada's defence spending to the student of our national affairs is undeniable. This article has discussed, in broad terms, the steps involved in the purchasing of stores, equipment and construction, currently totalling about $1,100 million per year. The cost of military and civilian pay, operations and Nato ($734 million); administration of Defence Production, Defence Construction (1951) Ltd., and cost of Crown-owned capital assets for the use of defence contractors ($22 million), raise the total spending to $1,856 million. This is equal to 40% of the $4,528 million covered by the federal budget for 1956/57, and demonstrates the cost of creating, expanding and maintaining a modern defensive system, in the air, on land and sea. These substantial costs arise from Canada's obligations not only at home, but overseas, as a member of Nato and United Nations. The importance of these obligations is well realized by those responsible for the business of defence spending, whose aim is to provide the armed forces with what they need, when they need it, and at the lowest cost consistent with the quality demanded.

CANADA'S ECONOMIC PROSPECTS

A review of the recommendations contained in the Preliminary Report of the Gordon Royal Commission on Canada's Economic Prospects

W. A. MACKINTOSH

THE PRELIMINARY Report issued in January by the Royal Commission, of which Mr. Walter L. Gordon is chairman, is a public document of great interest which seems likely to fulfil its intention of promoting sound thought on a number of specific problems and of increasing the interest with which the full report of the Commission is awaited.

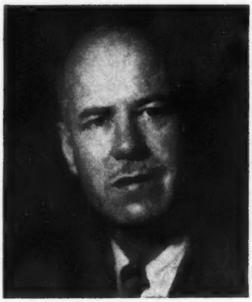
Such a preliminary report is in itself an interesting experiment in that it forecasts the final views of the Commission and offers them for public discussion before the full report is available. Possibly the Commissioners had in mind that the reports of the Rowell-Sirois Commission appeared simultaneously in such overwhelming volume that the public, even apart from the pressing concerns of war, was never able to master them in full. There would seem to be a good chance that the method adopted by the Gordon Commission will be conducive to more deliberate and fruitful public discussion. There is also an advantage in that the views of the Commission are made known while Parliament is in session.

These are great advantages but we should not lose sight of the fact that the summarized predictions of the Commission will ultimately be less important than a deep understanding of the forces at work in this country and of the sorts of future changes which may confront us. Desirable as it is, the preliminary report may do a dis-service if it leads the public, the legislatures and governments to stop short of real understanding.

To a country which has struggled for over three hundred years with refractory resources, difficult transportation problems, enforced population-scattering and at times discouragingly low rates of growth, the sketch which the Commission draws of the next 25 years is exhilarating and, to most, attractive. It does not, however, hide the fact that with rapid growth, there are also serious problems. A population of 16 million may become close to 28 million by 1980. The value of all goods and services produced (gross national product), at present around $29 billion, may by 1980 have become $76 billion and this on the assumption that prices remain constant. The working force is likely to increase about proportionately to the population but it will be spread through industry and occupations in a different pattern. Agriculture is likely to lose its relative position. Re-

source-development and manufacturing will outstrip the average rate of output-growth but the service industries will show the largest increase in the working force.

This expansion of the economy is generated by the favourable world environment in which people will take at profitable prices the products and services we can produce, and will see opportunities for profitable investment in the resources which we have. To look at it from another direction, it is generated by the availability of resources which at the present stage of technical development have become usable with profit as they were not in earlier decades.


W. A. Mackintosh, C.M.G.

The members of the Commission see in this changing picture certain areas or factors which are dynamic and which, if not themselves the prime movers, at least are central in transmitting the forces of growth. These can be listed but to suggest an order of importance would be to misconstrue the interdependence among them.

The first of these dynamic areas is in the field of energy. A country's industrial advancement is to be roughly measured by the amount of energy per capita which it uses. Canada is a country which, in its central region, has lacked coal. Despite the widespread substitution of hydro-electric power for thermal power, this lack of coal has been historically a limitation. In the Commission's view, we are now in a period when the importance of coal is rapidly receding as that of petroleum and natural gas rises. Coal by 1980 will be less than half as important relatively in the larger economy than it has been recently. Petroleum and natural gas together will have about the same predominant importance as coal had in 1926. As the importance of coal recedes, our recent discoveries of petroleum and natural gas will flow in not only to take its place but to provide for the large expansion predicted. Despite the statements of others that in a few years all our sources of hydro-electric power will be used, the report forecasts a larger place for water power by 1980. The Commission does not give any large importance in the next 25 years to the development of nuclear energy. It apparently accepts the view that in the foreseeable future, this will be simply a source of thermal power, competitive only where other sources are scarce and expensive. It is likely to be of much greater interest to areas such as the United Kingdom with wasting coal resources and to remote areas far from competitive fuel sources.

A second great dynamic area in the Commission's view is metals. Expectations are based on mounting world demand, technological progress in the recovery and use of light metals and the indications that we have mineral resources much larger than those already identified. In 25 years from now our production of aluminum ingot may be five times as great as it is today. Iron-ore output may be four times as great in value, copper twice as great and nickel and uranium may equal copper in value if there is increased processing in

Canada. Lead, zinc and magnesium could be two to four times the present level while titanium and a number of the rarer elements may also make substantial contributions. It is not pointed out that the futures of lead and zinc are focussed somewhat dangerously on storage batteries and galvanizing. The industrial minerals, of which the most important is asbestos, are also likely to increase greatly.

The rapacious appetite of modern industry for metals and other minerals to produce building materials, machinery and consumer durables will shape the Canadian economy of the future.

Population, too, in the view of the Commission is a dynamic factor. Our unexpectedly high birth rates, plus a substantial immigration, are likely to bring an increase of about 400,000 a year in our population and an increase of about 125,000 a year in our labour force. Whether considered as producers or consumers, this rapidly enlarged population is expected to be a dynamic influence.

Effects of Expansion

Much of the opportunity for expansion in the Canadian economy in recent years has come from technological advances which have made our metals needed and available and have enlarged the future of our chemical, oil and electrical industries. Some of the techniques we have developed ourselves. A great deal of the knowledge and know-how has come from abroad. Throughout the report, repeated emphasis is laid on the urgent necessity of enlarging our own sources of technical knowledge and developing our own technical personnel.

The expansion growing from these sources will be shared in greater or less degree by industries and regions and will have uneven effects in many quarters. Our forest industries seem likely to be up to the average rate of expansion and the Commission shows no concern for sources of supply. Along with resource industries and service industries, secondary manufacturing will contribute a larger share to the total output of 1980 than now. Then as now, however, it will depend almost wholly on the domestic market and will have to make headway against the mass-production of the United States and the low-wage, low productivity and competition of Europe and Asia.

Agriculture is expected to recede relatively, and be less than half as important in 1980. It will become more and more dependent on the home market and shift toward livestock products. It will, by increasing mechanization and scientific farming, increase its product while continuing to contract its manpower.

The uneven effects of this expansion will be shown regionally, particularly in the Atlantic provinces where hitherto resources have been limited and the great ports have had no hinterland adequate for their development. Though this is by no means the only area which may lag, it is apparently in the Commission's view the most important of such areas, and a good deal of space has been devoted to making tentative suggestions concerning its likely problems.

The Commission, as required by its terms of reference, has made extensive forecasts, all of which promise great growth in the Canadian economy over the next 25 years. The forecasts are illuminating and clarifying. They help us to see relationships.

They do not disclose any sharp change in direction. The same extension of resource development, by which wheat, pulp and paper, base metals and energy-using metals and chemicals were added, is to continue. What is striking is not the direction of growth but its predicted volume and speed.

As far as one can judge, these forecasts are made systematically and competently. The Commission wisely cautions us against placing too great reliance upon them. "The only thing that can be said with certainty about such forecasts is that evidence will prove them wrong, at least in part." Forecasts are useful and necessary as surveys of the future. They are made, however, only in the light of existing knowledge and understanding. Policy must always provide for evidence which is not yet available. More specifically, policy must provide for action or scope for action in the event that forecasts turn out to be wrong. Some are sure to be wrong, not because evidence has been ignored but because the evidence of the future is not yet known.

The real purpose of the preliminary report is to explain certain considerations of policy which have been brought to the Commission's attention in the course of its work, and about which it has felt prepared to make recommendations or suggestions.

Problems of Tomorrow

What are some of the urgent problems of expansion? What do we need to watch carefully? Out of what familiar ruts of thought should we be jolted? Where should we stimulate development? Where should it be curbed or spread over a longer period? Where are we failing to husband the seed-corn for the future? Are there regional or industrial sectors which will be injured by growth elsewhere?

Broadly speaking, the Commission has been deeply concerned that the expansion of our economy should be a Canadian expansion in the sense that it serves the Canadian people, strengthens our future position and enriches our national life. A number of its recommendations are directed to removing obstacles to expansion and making sure that the full limits of its forecasts are realized. It has been concerned also lest some industries and areas should not share in the expansion and that their futures should be jeopardized. It has given particular attention to, and forceful expression of, its views on the critical problems of human resources.

Most of its recommendations fall into the first category. Thus the recommendation of an Energy Commission to advise the Federal Government, and the provinces if they so desire, concerning the promotion of the best use of our energy resources arises from the view that in dealing with foreign corporations and governments, our own companies and provincial governments need strengthening. This and other recommendations would also seem to reflect a change of climate on the sacred subject of conservation, or at least a view that the conventional principles of conservation do not apply to waterpower, oil, gas and metals. They continue to apply presumably to drainage basins, forest growth, soil and fish resources. For the former group, however, the rapid change of technology and the rate of discovery of competitive resources would seem

to dictate the use of our energy and metal resources while they are usable.

The recommendation of an Energy Commission and extended export of energy are likely to be among the most keenly debated recommendations.

The suggestions in regard to taxation which appear in several parts of the Report all seem to be directed either to encouraging investment or to removing any differential advantages which the foreign investor may have. These taxation proposals could be discussed only in much greater space than is warranted here. The Commission's endorsation of liberal and flexible depreciation allowances is a reminder that as long ago as 1938 a modest installment of this policy was recommended by the National Employment Commission of which the late Arthur Purvis was chairman. The changes which have taken place since then and the recommendation of the Gordon Commission are welcome evidence that the views of accountants, lawyers and civil servants do change, if slowly.

Views on Foreign Investment

In its consideration of capital investment and the significance and risks of foreign investment, the Commission wisely points out that the main advantage of the foreigner over the Canadian is not simply or chiefly the possession of capital nor the willingness to risk it. It is in the ability to provide a package made up of technical knowledge, markets and venture capital. There are some suggestions for enlarging Canadian sources of capital by relaxing the restrictions on trustee and insurance funds and, somewhat vaguely, the development of new mechanisms for concentrating venture capital. There are, no doubt, useful things to be done here but they will not yield spectacular results unless markets and technical knowledge can also be provided.

The Commission shows some concern that foreign investments should be highly concentrated in certain industries and that they should be almost entirely equity investments. There seems to be a yearning for earlier decades when most foreign investments in Canada were of the fixed-interest type. Since most of us now have our eyes fixed on the 25 years ahead, it is worth recalling that 25 years ago Canadians were bemoaning the rigidity which her foreign-held bonds gave to her balance of payments. It is a mark of the change in attitude and circumstances that the flexibility of equity investment is now less important to us than the question of control of industry.

The Commission has taken account of the pronounced and rather definite public opinion in this country favouring greater Canadian participation in, and a progressive policy of naturalization of, foreign-owned subsidiaries. Fairly general agreement can be expected on the recommendation that such subsidiaries should become Canadian institutions having Canadians in some at least of their senior positions, publishing statements on Canadian operations and promoting the issue of at least 20% to 25% of their equity stock in Canada. These are steps which foreign subsidiaries are held likely to take because of their value in public relations, and because any tax advantages, which there might be in other courses, will have been eliminated. On one point the Commission is quite clear and firm: it recommends a limitation on the vot-

ing power of foreign owners of Canadian bank and insurance stocks.

It is clear that the Commission found no novel and dramatic answer to the problems of the Atlantic provinces even though it calls for a positive and comprehensive approach to the problems of this region. It bespeaks a generous and constructive attitude to the problems of inadequate resources, the impact of mechanization and the modernization of transportation. The proposed Joint Capital Projects Commission, which merits consideration, is really a device for using federal funds to induce a functional union among four units, none of which is large enough to cope with such problems alone.

No one associated with universities can be other than heartened by the concern of the Commission to extend and raise the whole standing of our universities. Its members see rightly that not only are much larger numbers of students coming forward but our chance of maintaining our national status in reality will depend on trained persons, equal in capacity, in scientific training and in perspective to the best that other countries can produce. They recommend the provision of what appear to be large sums of money to raise salaries, to provide buildings and equipment and to furnish scholarships, bursaries and loans for students. "What is being suggested in essence is that a deliberate and sustained effort be made to raise the quality and standards of Canadian universities to among the highest prevailing anywhere in the world." It is rightly pointed out that the sums required are moderate in comparison with those obtained for construction projects and social security.

Only the preliminary report of the Commission has appeared. Its recommendations and suggestions will raise some controversy and, it is to be hoped, much discussion. The final report and the studies should provide the basis for fuller understanding and deeper insight into the problems which growth imposes on us. There is some danger current that the impressive growth of the past ten years and the great expansion promised may lead Canadians and others to think that this is an easy economy to develop. The currents, winds, and tide of population growth and market demand, technological advance and resource-discovery seem to sweep us on our way toward the horizon of 1980. In fact, it has been and will be a difficult economy to develop to satisfying standards of unity, independence and stability. The Canadian climate no doubt engenders vigour but imposes some costs and handicaps. Once we have occupied the arable land, cut the accessible forests for timber and sawn lumber, carried out simple quarrying and smelting operations and taken fish with schooner and dory, the further development of our resources requires a complex technology and massive investment. Our population, here concentrated in great urban aggregations and there scattered thinly and unevenly over immense areas will require high standards in services. The currents of economic change will affect different parts of the country in varying degrees, and some from time to time adversely. It has not been by predilection but by the logic of its experience that the Commission has come to lay such great emphasis on the development of our human resources.

The Review of Internal Control and the Audit Program

W. E. SHIELDS

DURING THE LAST generation the nature of an audit examination has changed considerably. In the first part of this period it was not uncommon for the auditor of a business to examine the records of virtually every transaction. However, over the course of the years several factors have tended to change the extent and scope of the examination. Businesses have grown and have become more complex, and management has required detailed and frequent interim operating statements. As a result, capable and experienced accountants, trained in many cases by accounting associations and institutes, have been employed. With the advent of larger and more experienced accounting and bookkeeping staffs, more internal checks on recording of transactions were possible within the businesses themselves. These provided protection at lower cost than detailed audits by the external auditors. As a result the audit today usually consists of a test of the transactions for one or at the most three or four months during the year, a scrutiny of the transactions for the remainder of the year, and the normal verification of the balance sheet at the year end.

However, once the auditor departed from the detailed audit it became necessary for him to make a critical analysis of internal control in order to justify the change in emphasis. He was also faced with the problem of making an intelligent decision as to the areas in which he should concentrate his audit tests, and the extent of such tests. This paper is concerned with a method for evaluating internal control and relating the audit program to the weaknesses and strengths in internal control which have been so revealed.

Ascertaining the Nature of the Internal Control

In relating the internal control system to the audit program it is necessary first to ascertain the nature of the internal control supposed to be in existence, and there are various methods of doing so. For example, the auditor may merely make an informal review of internal control or he may use a questionnaire or check list. Whatever method he may use, it can only be effective if he is conversant with the underlying system from which the internal control is derived. The method which is described in the following paragraphs is founded on the review of the system and internal control as one integrated operation.

As it takes a measure of experience as well as tact to review a system of internal control successfully it is preferable that this review be carried out by a senior member of the audit staff. In the case of larger clients the reviewer might well be the audit supervisor or partner himself. Before the interviews with the client's personnel are commenced the auditor should have at least a working knowledge of the client and his affairs. This can be acquired by making a trip through the plant and observing the physical layout, noting how the products are handled, and scrutinizing the supplementary records maintained outside the accounting department. He might also obtain an organization chart showing the duties and responsibilities of senior officers and employees of the company. As he is particularly concerned with the accounting department, he might make a rough list of the accounting personnel showing their duties and the records for which they are responsible. After this general information has been obtained the auditor can commence his formal review of system and internal control.

Usually it is best for the person undertaking the review to visit initially the most senior financial officer of the company who has a working knowledge of the accounting system, and to obtain general information about the system in use. The information obtained is important as it indicates the executive's conception of what is being done by the accounting staff. Next, the interviewer should visit the various section heads, and ultimately various members of their staffs in order to check his information and to obtain further details of the actual operation of the system. In some instances it may be necessary to interview other executives for ancillary information. Frequently there are variances between what the executive thinks is being done in the accounting department and what is actually taking place, and the uncovering of these discrepancies is really the first benefit of the review.

In any business the various transactions follow in a logical sequence or flow. For example, the customer places an order, the order is approved for credit, the goods are shipped, the customer is invoiced, the invoice is posted to the accounts receivable ledger, and ultimately cash is received in payment of the account and recorded in the cash receipts record. The flow of transactions forms a pattern and the effectiveness of the review is enhanced if the questions which the auditor asks the persons he is interviewing follow this sequence. During the course of the interviews weaknesses in internal control will become apparent and the interviewer should direct questions on this subject where necessary. It is possible, however, that weaknesses which become apparent during one portion of the interview may prove to be nonexistent because of controls in another sector of the system. For example, the failure to prenumber and account for all sales invoices issued may be unimportant if the company regularly reconciles its total goods invoiced with production and stock on hand.

Preparation of a Memorandum

During the discussions the person undertaking the interview should make notes for incorporation in a memorandum. The memorandum is a record of the system and internal control in force and can be used as a

basis for determining the direction and extent of the audit procedures to be undertaken. If, at some future date, a decision must be made as to a change in the audit procedures, the memorandum can be used to refresh the memory of the auditor. Also if there are changes in the audit staff it is useful as a guide to the new personnel doing the field work.

The logical form of the memorandum is in two columns, the first describing the system of procedures and the second, side by side with the first, outlining the weaknesses and strengths in internal control relating to the system. The notes on system and internal control, like the review itself, should follow the flow of transactions and for purposes of clarity be in point form. It is often useful if some portions of the system are illustrated in graphic form. Where an internal control check list is available, it is useful to review the system notes in the light of the check list in order to ensure that all the possible weaknesses have been revealed. The form of the memorandum is illustrated by the following example:

A. B. C. COMPANY LIMITED

MEMORANDUM RE REVIEW OF SYSTEM AND INTERNAL CONTROL

System	Internal Control Weakness
SALES:	
Records —	
1. File of accounts receivable and sales summary invoice copies in numerical order by month.	
2. File of shipping orders showing cost of goods sold — filed in numerical order by month.	
3. For each customer, a folder containing copies of invoices to him.	
4. Adding machine tapes of sales summary and accounts receivable invoices copies by type of goods sold.	
5. Adding machine tapes of shipping orders by type of goods sold.	
6. All entries to general ledger are made through *recurring journal.*	
System —	
1. Customer's order is accepted by storekeeper. He writes a memo on a form (not pre-numbered) which is passed to the invoicing clerk.	1. See 3. below. In addition there is no guarantee customer's orders are filled.

A. B. C. COMPANY LIMITED

MEMORANDUM RE REVIEW OF SYSTEM AND INTERNAL CONTROL

System	Internal Control Weakness
2. From information on the memo, the invoicing clerk types in customer's name and a description of quantity and type of goods ordered (on a prenumbered invoice blank in six copies) (1) Original (white) – customer's copy (2) Customer's file copy (green) – for customer's folder (3) Posting copy (pink) – sales and accounts receivable posting (4) Shipping order (yellow) – shipping and cost of goods sold and inventory (5) Packing slip (blue) – packed with goods when shipped (6) Sales breakdown – customers service (orange) – to sales manager's secretary (#6 copy not used for accounting purposes) Invoicing clerk removes copies #4 and #5 and passes them to storekeeper.	
3. Storekeeper ships goods enclosing packing slip (#5 copy) and enters on the shipping order (#4 copy) the quantity and date the goods shipped. He does not initial the shipping order. Shipping order is then returned to the invoicing clerk. Where the sale is a cash sale or a sale to an employee, the storekeeper frequently delivers goods and then takes cash or a memo to the accounting office after delivery.	3. Person who accepts order also fills it, leaving a possibility of collusion with customer or omitting to advise billing department. On a cash sale, the storekeeper could pocket cash. Employee's purchase might not be recorded.
4. The invoice (copies #1, #2, #3 and #6) is completed as to date and quantity shipped, priced, extended, and added by the invoicing clerk. She mails the original copy (#1) to customer and passes copies #2 and #3 to accounting machine operator; #4 copy to inventory clerk and #6 copy to sales manager's secretary.	4. All pricing and extensions are done by one person and not checked, leaving possibility of fraud or error.

A. B. C. COMPANY LIMITED

Memorandum re Review of System and Internal Control

System	Internal Control Weakness
5. Inventory clerk posts shipping order (#4 copy) to perpetual records and enters unit cost on order. She extends and adds cost and summarizes cost of goods sold and inventory credit for the month. She does not account for serial numbers.	5. Shipping orders which were lost would not be discovered, resulting in incorrect costing of sales and incorrect perpetual records.
6. Accounting machine operator posts #3 copy to accounts receivable subsidiary ledger. She summarizes copies for posting to sales summary and accounts receivable control account. Sales are summarized by type of goods sold as there is a separate sales account for each product. She accounts for the serial numbers of #3 copy. After month's posting is balanced she returns #2 copy to invoicing clerk.	
7. Invoicing clerk files #2 copy in customer's folder.	
8. Where the sale is a replacement of goods returned as factory replacements, a special price is granted to the buyer. Invoices are made out at the regular price and a credit note issued for the difference between the two prices.	
9. Sales and cost of sales are entered in the recurring journal by the clerks who build up the summaries.	9. Entries are not made or checked by accountant, leaving possibility of error.

The weaknesses in internal control which are indicated in the memorandum together with any suggestions which the auditor may have for improvements in the client's system should be discussed with the client reasonably soon after the review has taken place. It is desirable that the results of this discussion be incorporated in a letter to the client.

Timing of the Review

There are several theories as to when the review should take place. For example, some auditors prefer to have it undertaken before audit work is commenced. Others claim that it should be done gradually as the work progresses and in line with the work being done. Obviously a formal review of system such as has been described here is a time consuming process, and this creates a real practical difficulty. However, once such a review has been accomplished the auditor and his staff should have the system in mind as they undertake

their duties so that in effect a continuous review is performed. In the writer's opinion there are advantages in undertaking a formal review of the entire system once every two or three years, the frequency being dependent on the rate of change in the accounting system. In the intervening years the audit staff could make changes on a copy of the memorandum on system in order to keep it up to date.

The Audit Program and Audit Sample

Once the system review has been completed and the resultant notes on weaknesses on internal control have been made, the audit program can be prepared. The tests outlined in the program should be designed to accomplish two things. First, it is necessary to prove by audit procedures that the controls which the system notes indicate to be in existence are in effect. Second, when the system is weak by its nature, as revealed by the notes on weaknesses in internal control, or has broken down, it is necessary to extend the applicable audit procedures until the auditor is satisfied that there is little chance that any substantial fraud or error has occurred. When preparing the program it is necessary to differentiate in emphasis between those procedures which are used to determine whether or not the system of internal control said to exist does in fact exist and those used in making tests in areas where internal control is known to be weak. In the former instance, there should be more emphasis on observing the actual procedures themselves and scrutinizing the entries in the books of account rather than an exhaustive examination of original documents. In the latter instance it will be necessary to audit individual transactions in sufficient number to ensure that there is little likelihood of significant fraud or error.

As has been mentioned above, the extent of the test of individual transactions should be governed by the degree of internal control in existence and the tests should obviously be extended where the internal control is weak or where a number of errors have been discovered. The selection of the size of the sample to be tested is a matter of judgment made after considering the client's system of internal control. Some sources have advocated the use of statistics as a tool to be used in the determination of the size of the sample. However, in most cases the individual transactions which are to be examined are not homogeneous in nature and this limits the effectiveness of statistics. Also the auditor must still exercise his judgment in deciding whether or not the percentage of probability that the sample actually represents the whole mass of transactions is acceptable for audit purposes.

Assuming that a reasonable sample is decided upon in the light of the internal control in effect it is still necessary to make a selection of the transactions to be checked. Generally speaking, if the auditor is interested only in significant errors which might affect the financial statements, the larger transactions will be examined. If, however, the purpose of the audit is to see whether or not the client's staff are committing errors, no particular attention would be paid to the size of the transaction. There is really no easy dividing line between the two methods of selecting transactions to be tested and each test should be carefully examined before

deciding whether or not particular attention should be paid to the larger items.

Advantages to a Review of Internal Control

There are several advantages to the type of review of systems and internal control which has been described in preceding paragraphs. It provides detailed and accurate information on the accounting system and reveals the flow of transactions in logical sequence. As a result, weaknesses in internal control can be more easily ascertained and the audit effort can be more effectively directed to those areas where the weaknesses exist. At the same time where it is apparent that the internal control is effective, the extent of the interim audit can be reduced to a point where it is only necessary to prove by audit procedures that the controls are actually working. In some instances improvements in the accounting system itself become apparent and can be suggested to the client.

The most significant disadvantage, of course, is the amount of time required to undertake such a review and this disadvantage must be weighed against the benefits derived from the increase of the effectiveness of the audit itself and the reduction in detailed work made possible by being in a position to rely on the system of internal control.

FINANCIAL PLANNING

Failure to look ahead places a business in a risk enterprise class. The test to apply is — are we best utilizing the resources at our disposal in relation to conditions now and possible conditions in the future? Some initial impulse in the matter of future activities will come from top management in the interpretation of company policy, but a constant survey of the utilization of the company's resources falls properly within the province of management accounting.

—From "What the Industrialist Wants from Management Accounting", by G. A. Boardman, *The Accountant*, Dec. 29, 1956.

Integrated Data Processing - A Case History

A. A. MACKEY

DURING THE past several years in particular, the Canadian National Railways has been carrying out an intensive program directed at increasing the effectiveness of its clerical and accounting operations. The object of the program, which is being carried out simultaneously in a number of different facets of the company's operation, has been to devise means of providing more useful statistical and control information at lower cost.

The payroll operation was the activity at which the first major study was directed, the principal reasons for this priority being:

1. It is a very large operation involving great masses of complex but fairly repetitive work, all of which must be performed within a tight time schedule. The Canadian National, which employs some 117,000 people in Canada, is in fact the largest employer in the country apart from the government.
2. The payroll offered no particular problem by way of defining output requirements, the principal requirements in the first phase of mechanization being nothing more than pay cheques and payrolls.
3. The payroll operation could be isolated and contained in an homogeneous package in the first instance, yet it also afforded an excellent base from which to integrate progressively the processing of all media pertaining to manpower accounting, i.e. payrolls, cost distribution, operating and capital budget control data, pension records, staff records and personnel statistics.

The general sequence which was visualized when the study was first undertaken was:

1. Conversion from manual methods to conventional tabulating equipment accompanied by a relatively minor degree of integration, i.e. payrolls, cost distribution, pension records and a minor amount of statistical data.
2. Progression from this base to full integrated data processing utilizing medium sized computing equipment, accompanied by the progressive decentralization of the clerical timekeeping functions with the consequential establishment of data input centres at a number of points across Canada.

It has not yet been determined

whether the use of a large sized computer is desirable for this operation alone; at this point it appears doubtful, but it does seem probable that in due course the payroll operation will become one of several users of a large computer.

The case history which is set out here describes successively the planning and implementation of the first phase referred to above, i.e. the conversion from manual methods to conventional tabulating equipment from inception to completion, and the steps which have been taken to this point in preparation for progressing into the second phase. These histories are prefaced by a brief description of the nature of Canadian National's payroll operation by way of bringing the programs into perspective.

Scope of Payroll Operation

As mentioned above, the Canadian National employs approximately 117,000 people spread across the country from Newfoundland to Vancouver Island. For the most part these people are paid by cheque on a semi-monthly basis. They work at some 260 different trades, and because of the many variants in wage scales, basic pay plans and arbitraries, as well as the fact that there are in the order of 300 different payroll deductions, the actual computation of the payroll is unquestionably one of the most complex large scale accounting operations in Canada.

The general format of the operation is that the basic pay media (such as time reports, clock cards and trip tickets) are originated at some 6,000 points in Canada and despatched to the appropriate regional offices (or district office in the case of Newfoundland). The time and rate checking is carried out in these central offices, following which gross pay is extended, deductions applied, net pay determined, cheques and payrolls prepared and the cheques and pay lists divided up and despatched to the 6,000 pay points at which the basic media was originated. The number of employees whose pay is cared for by each of these offices is approximately as follows:

Toronto	(Central Region)	57,000
Winnipeg	(Western Region)	37,000
Moncton	(Atlantic Region)	17,000
St. John's	(Newfoundland Dist.)	6,000

Slightly under 3 million pay cheques are issued each year.

At the inception of the project the payroll work at all Canadian offices other than Toronto was cared for by manual methods supplemented by conventional office equipment such as comptometers, desk calculators and typewriters. The Toronto office payroll was cared for manually up to the point of calculation, at which stage the variable data were mark-sensed onto a tabulating machine card; tabulating equipment was utilized for the calculating and printing processes and for the production of deduction lists, etc. The Toronto system which had been installed in 1948 had not lived up to expectations, primarily because machines had been substituted for one major phase of a manual operation and had not been molded into the entire process. In retrospect, from which vantage point most judgments are infallible, it was clear that if machines were the answer the massive flows of raw media should have been tailored more precisely to meet the machine requirements.

It was decided that the initial study should be undertaken in Toronto, not

only because this office contained the largest of the payroll operations and was the closest office to Montreal headquarters but also because the first machine application had not met expectations. It was considered that a marked improvement in the operation of this office represented a psychological prerequisite to successful methods improvements programs in other offices and other accounting activities.

The Survey

Before the methods group was established to commence the survey, a management consultant was engaged to make a methods audit with the object of identifying the aspects of the operation which seemed to offer the best possibilities for improvement and indicating generally the form which the improvement should take. This audit was made quickly and was not detailed but as the company methods survey progressed, it proved to be very accurate and it provided an excellent set of reference points for maintaining an overall perspective.

The first company methods team, which comprised five people, was formed at the beginning of 1954 and an approximate time table was set up. This schedule required completion of investigation and presentation of recommendations as to methods changes by the spring of 1955. A period of approximately nine months was left for procuring equipment, designing forms, writing detailed procedure manuals and for the extremely important training activities which would have to be completed before the target dates for installation, which were tentatively set at January 1, 1956 for Toronto, April 1, 1956 for Winnipeg and July 1, 1956 for Moncton; no immediate change was planned with respect to the Newfoundland operation.

All of these target dates were met, although they were set some two years in advance by exercising judgment on the facts disclosed by a general assessment and although a very large and complex retroactive pay requirement arose during the early stages of implementation at Winnipeg and Moncton.

Several basic principles were established at the inception of the survey, notably:

1. Since this was the first major effort of this type in the Canadian National, it was vital that natural fears of the unknown should be resolved as much as possible. To this end the employees' union representatives and the employees themselves were advised that:

   a) The object of the survey was to improve the efficiency of the operation and to reduce costs through reductions in staff.

   b) However, no employees would lose their positions by reason of the survey or of the new system which was expected to result therefrom because it had been established that the rate of normal attrition would be more than sufficient to care for staff reduction without lay-off.

   c) The improvements which it was hoped would be developed would accrue to the benefit of the company, but they would also benefit the employees, primarily because although a number of lower paid clerical positions would be eliminated through the process of attrition, there would also be an increase

in the number of higher-rated positions. Apart from the immediate financial incentive, these new positions would afford an opportunity to acquire skill and experience of a type which would be in great demand inside the Canadian National as the company program developed and for which there would be an increasing demand in other Canadian companies.

2. Every effort would be made to avoid the stigma of "efficiency expert". It was imperative that the confidence of line supervisors be gained and that these supervisors participate in the program, not only to provide information and suggestions, but also to ensure that the people who would have to bear the major share of the burden of installing and operating the new system would be under the psychological compulsion of ensuring the success of a system which they had helped create.
3. Every possible opportunity would be taken of apprising as many people as possible of the progress and current status of the program.

It would have been unrealistic to expect that application of these principles would be fully effective but experience demonstrated that this approach was of major assistance in gaining acceptance for the survey group and for the changes incidental to the installations themselves.

The survey itself followed the fairly well established pattern of detailed investigation, flow charting and synthesization. It became apparent in January 1955 (about one year after inception of the survey) that the final answer involved a complete redesign and standardization of forms and paper flows and the application of a high degree of mechanization to the massive mathematical task of applying pay variants to pay constants and to the process of assembling and printing the various payroll documents. It was also clear that it would be impracticable to revise the clerical paper flow processes and to install mechanization as separate projects by reason of the high degree of integration which would be required. Thus, although the mass and number of variants involved in the calculating processes were such that the use of a medium type computer was indicated, it was decided that as a practical matter it would be unwise to install machines which would be as intolerant as computers of this class.

To put this another way: it was decided that the paper flows should be so designed as to ensure compatibility with computer requirements but that relatively tolerant machines should be used until such time as the effectiveness of the newly-designed paper-flows could be proven both as to content and timing, and the normal (and unavoidable) vagaries overcome.

Another reason for making this decision was that very little machine skill or experience was available within the company. It would be necessary to select and train in the order of 200 people in key punch, machine operator and machine supervisory skills. The results of this training program could not be relied upon to the degree necessary to attempt a computer installation as a first step.

The results of the survey and these practical considerations made it possible to take a final decision in February 1955. The elements of this de-

cision may be summarized as follows:

1. The paper flows would be completely re-designed with the object of simplification and standardization. The re-design would be directed specifically at the needs of a conventional tabulating installation but it would also be compatible with computer requirements.
2. Complete procedure manuals would be prepared to govern the preparation of these forms (at 6,000 field points) and their subsequent processing in the three regional offices.
3. Production planning and control principles very similar to those applied in manufacturing operations would be applied with respect to clerical processing of these forms in the regional offices.
4. The machine process and forms would be so designed that from the point at which the punched card is first produced by key punch it would be practicable to substitute a computer with direct printer output for the sorting-collation-calculating-printing process envisaged in the first installation with a minimum of revision in the principles of processing.
5. The original installation targets could and would be met, i.e. Toronto on January 1, 1956, Winnipeg on April 1, 1956 and Moncton on July 1, 1956.

At this point preliminary machine specifications were written, machines were ordered and detailed plans were made for carrying out each of the decisions enumerated above.

Planning the Installation

The relatively small methods group (of five) was supplemented at this stage by approximately 25 people from the line organization and the character of the group changed from a survey group to an installation team. This would be described more accurately as a group of installation teams since it was possible to break the project down into specific assignments and detail a group to deal exhaustively with each of the assignments. One group, for example, cared for the redesign of the basic time media forms, the writing of the detailed procedures to be followed by field personnel in using these forms and for the instruction of field personnel. At the same time other groups were dealing with such matters as design of forms for the machine process, machine programming, control panel wiring and the selection and training of machine room personnel.

The installation planning was carried out mainly in Toronto but the teams included personnel from the other two regional offices; the membership of these teams kept changing as the planning progressed and the emphasis on different aspects of the installation changed. This approach had several advantages apart from the fact that it afforded the only feasible means of caring for the heavy volume of work which was involved, the principal ones being:

1. Personnel with substantial responsible experience in the specific types of work could prove or disprove the validity of the proposals and they could write detailed instructions from the base of a solid background of experience.
2. These men, who would later carry major installation responsibilities, would acquire thorough knowledge of the new processes, would

be satisfied as to their effectiveness and would be able to plan the details of installation in their home regions.

3. It afforded a means of disseminating information regarding the new system.

Coordination of this planning process proved to be quite difficult, in part by reason of the technical difficulties of the work itself but also because the planning was being carried out simultaneously for all facets of the work for three separate areas. The planning was, nevertheless, completed successfully and on time.

Implementation

Implementation proceeded generally according to plan but in the Toronto operation in particular it became apparent very early in the implementation process that the impact of the change was even greater than had been anticipated. The new system was a tightly integrated package and failure to carry out one phase effectively and on time would compound the difficulties in the next phase and in the final analysis major difficulties would be encountered in the final machine processes. This was known from the beginning and substantial tolerances were built into the system for protection during the transition but these proved to be insufficient and serious difficulties were encountered. The reasons for these difficulties may be summarized as follows:

1. By reason of the basic changes in forms, data arriving from the field points (of which there are some 3,000 in the region serviced from Toronto) tended to arrive late and to contain an incidence of error which was tolerable and correctable in a manual process but not in a machine process.
2. The forms and the clerical phase of the accounting process were also new to the regional office personnel and although these people had been given training in the new system and had substantial experience in payroll work, the lack of actual experience with the new forms and the new process and the deterioration in quality of the material received from the field points slowed down production and lowered quality.
3. The media thus reached the Machine Bureau later than planned and in less satisfactory condition than expected. At the same time the Machine Bureau personnel were confronted with the task of winding up the previous year's work under the superseded system and naturally lacked practical experience with the new system. The situation was complicated further when several of the machines developed mechanical difficulties beyond the degree for which allowance had been made.

Provision had been made for all of these difficulties and the existence of the compounding effect was well known in advance but the degree was greater than expected. The system itself, however, proved to be technically sound.

The difficulties associated with production of the first payroll were overcome in part by ingenuity but mainly through sheer massive effort on the part of the office staff. This effort was put forth willingly and it stemmed from a combination of pride and loyalty and without it the transition would have failed despite the technical soundness of the new sys-

tem. As indicated earlier, the offices are organized; the union officers worked closely with the company and their cooperation and assistance during this difficult period contributed greatly to the final success of the transition.

Personnel from the Winnipeg and Moncton offices were present in Toronto during the implementation period, in part to assist but more particularly to observe the actual difficulties encountered and to take steps to avoid them in the other regions to the extent possible. The result was that when the new system was installed in Winnipeg and Moncton the transitions were accomplished with relatively minor difficulties although, as could be expected, new difficulties emerged which were peculiar to each of these points.

Progression to Full I.D.P.

The conversion from manual methods to conventional tabulating methods was successful from the point of view of economics but also had these ancillary advantages:

1. It provided an opportunity for developing and disciplining a paper flow process compatible with the needs of computers without imposing the rigidity of computer requirements during the initial period.
2. It provided a training period for methods, clerical and machine personnel and in fact created a pool of skills not previously available within the company.
3. It demonstrated that massive and complex changes could be accomplished and it established a firm base for the next step.

The change which has been accomplished probably ranks among the most difficult of its type yet carried out in Canada, but the development of the current system into a computer operation does not present equally complex problems. The basic reason is that the punched card used in the current system is a constant, which means that so long as this constant can be maintained in terms of both content and time the clerical processes which precede creation of the card and the machine processes which utilize the card can be altered independently of each other.

Investigation of the computer potentialities had indicated that substitution of a medium sized magnetic drum computer with direct printer output for the conventional machine processes would be attractive economically and would have several ancillary advantages, notably:

1. It would speed up the machine processes thus flattening off the payroll peaks.
2. It would make it feasible to accomplish a higher degree of integration of the payroll process with the other facets of manpower control accounting.
3. It would provide a good economic base for a computer service centre into which other applications could be introduced at the appropriate time.

For these reasons decision was taken in June 1956 to apply a computer to this operation and equipment was ordered for delivery in June 1957. In the first instance the computer will care for the Toronto payroll only (57,000 employees) and it is economically sound on this basis, but it also has sufficient capacity to care for the payrolls now processed to completion in the other offices.

Programming commenced in September 1956 and is proceeding according to schedule. Logical block diagrams (which constitute gross proof of the logic of the process) have been completed and the more difficult and time-consuming detail programs have been completed and checked out. The four programmers who are engaged in this work were selected from within the company and were trained in programming; the initial programming, which includes training periods, is expected to consume about 36 man months.

This case, which has involved the installation of some of the most advanced machines actually processing accounting work in Canada today, has been a most interesting and rewarding experience for all who have been associated with it but these machines will be supplanted shortly by more advanced equipment now being readied for installation by the Canadian National and by other companies. We consider this to be a normal development during a period of technological improvement and we believe it to be a good practical demonstration of this evolutionary process.

This case has taught us many things and has reconfirmed our belief in other things. We have learned that the only real experts in this work are those who have never carried the responsibility of an installation; after that you are no longer an expert. But more significantly we are more convinced than ever that people are the most important part of any systems change and that it is scarcely possible to spend too much time in explaining your plans and intentions to the many people who will be affected and in the detailed training of those who will be engaged in the changeover itself. Our experience also demonstrates beyond question that integrated data processing can progress only as rapidly as new skills can be learned by people who are at work today. This is by way of saying that the progress may well be much slower than was originally expected because these new skills are very complex indeed.

On the other hand the unprecedented upgrading of office skills which is entailed will be one of the major factors in gaining the social acceptance which is a prerequisite to the success of this evolution.

Preparing Tax Returns by the Diazo-Type Process

C. F. GAVILLER

THERE IS, as has been said before, a business aspect to the practice of any profession, and public accountancy, with its rapidly expanding firms, increasing variety of services offered and mounting volume of paper work, is no exception. It seems only reasonable that the more efficient this business aspect is, the higher will be the quality of professional service, for then the mind is free to concentrate on the things that matter, uncluttered by mechanical problems.

One such problem, which requires a disproportionate amount of time of many accounting firms, is the reproduction of income tax returns and related financial statements and schedules. If a firm has a large number of clients, operating unincorporated businesses, this problem seems insurmountable especially during the period January 1 to April 30. Yet there is a solution to it—the use of Diazo-type reproduction equipment.

Different from Photocopy

A distinction should be made between the Diazo-type process and the photocopy process. The latter requires that a negative be made first, and from this the copy is printed. With some exceptions each negative will reproduce just one copy and reproduction requires about one minute per copy. Originals must be on opaque not translucent paper.

The Diazo-type process does not use a negative but prints directly from the original. It requires that the master be on translucent paper; originals on opaque paper require an intermediate process. Any number of copies, called "prints", can be made from the master at the rate of a few seconds each. The print is delivered from the machine dry and ready for use.

The advantages of the Diazo-type process in the mass reproduction of tax returns and related financial statements and schedules are its speed of reproduction, simplicity of operation and the inexpensiveness of the paper used. Photocopy equipment is preferable where few copies are needed, usually one, and the original is on opaque paper, e.g letters, agreements, by-laws, magazine articles, assessment notices, etc.

Process of Reproduction

To produce a print by the Diazo-type process the translucent master is placed face-up on a sheet of sensitized paper and fed into a Diazo-type

machine. ("Diazo" is a commercial term derived from "diazonium salts", light-sensitive material used in the sensitized paper). The master and the sensitized sheet, held in close contact, are carried on belts past an ultraviolet light tube to which they are both exposed, the master then emerging from the machine, the sensitized paper carried on through the developer and the heat-drying process to be delivered as a finished print. As soon as the master has been returned by the machine, it is matched again with a sheet of sensitized paper and fed back into the machine for another print. There is no need to wait for the delivery of a finished print before the master is re-inserted. Masters matched with sensitized paper can be fed in at a rate governed only by the dexterity of the operator. There may be ten or more potential prints in the machine at one time, although not all would be developed from the same master. This means the machine will deliver at the rate of ten or more finished prints each minute. The translucent master may be handwritten or printed with pen or soft pencil or may be typed. Since blue pencil markings on the master will not reproduce in the print, a blue or violet non-reproducing pencil can be used for checking.

Governmental Approval

This process has been approved by the U.S. Treasury Department for the reproduction of tax forms for at least four years. In Canada its use in reproducing the T-1 General income tax return for individuals was approved with certain conditions in 1956. Technical difficulties relating to the Diazotype process and the colour of the form have so far prevented the reproduction of the T-2 return. There has never been any objection to reproducing financial statements and schedules for inclusion with T-1 or T-2 returns. The United States Treasury Department will accept a print of the official tax return form, while the Canadian Department of National Revenue will accept only the master of the return, although it will take prints of the financial statements and other schedules. Printed T-1 general forms are available on translucent masters at about 15c each. With greater use, lower costs might be anticipated.

To obtain maximum benefits from this use of the Diazo process, dummy balance sheets, income statements and capital cost allowance schedules should be pre-printed on translucent paper masters. In some cases it will be preferable to have translucent film masters, on which the pre-printed form remains fixed but the pencil figures can be removed very easily and a new set of figures entered.

Four Steps

Briefly the procedure for reproduction of a tax return and enclosures is as follows:

1. The assistant, working from his trial balance and work sheet, inserts by hand the figures on the pre-printed, translucent balance sheet and income statement forms to be used subsequently as masters. The other schedules of capital cost allowances, donations, etc., are prepared similarly. Finally, the tax return, a pre-printed translucent master, is filled in by hand. The assistant preparing the file initials each master, except the tax return, with a non-reproducing pencil. Since the Department of National Revenue requires that

the master be filed in the case of the tax return, a minimum of marking should be made on this form. A slip of paper bearing initials for preparing and reviewing can be attached to the master tax return and later transferred to the office copy of the print. The file is then passed to the reviewer.

2. The reviewer uses a non-reproducing pencil for his check marks and initialling. Corrections are made by erasing on the masters and rewriting in pencil. Again, prominent check marks should be avoided on the tax return. The file then goes to the machine operator.
3. The machine operator runs the file through the machine, obtaining two prints each of the return, financial statements and schedules. The prints are delivered from the machine dry and ready for assembly.
4. The machine operator assembles three copies of the file, the first for the tax department consisting of the tax return master and prints of the enclosures, the second for the taxpayer made up of prints of the tax return and enclosures and the third for the office file made up of a print of the tax return and the translucent masters of the enclosures.

A file of this kind, when run with other files, should take about five minutes to pass through the machine.

Advantages of the Diazo Process

Two advantages of this process over the typing method in the mass reproduction of tax returns are greater speed and reduced cost. It eliminates typing, proofreading, checking of additions and correction of typing errors. Some United States firms have reported reductions in typing staff of a third to a half after it was introduced into their offices. In one Canadian firm it has been found that a T-1 return, together with the balance sheet, income statement, capital cost allowance schedule and schedules of donations, medical expenses, etc., is reproduced (two prints of each) in about five minutes. Reproduction by the typing method, including time for proofreading and checking of additions, etc., would require about an hour and three quarters. Thus, the Diazo-type machine will reproduce 20 files in the time taken to copy one by the typing method. Material costs are very little more.

One need not be concerned about the appearance of the prints. If the assistant preparing the original work is a poor writer, he should hand print. Check marks and initials of the preparer and reviewer do not show up in the print if made with a blue or violet non-reproducing pencil. Clients are impressed with the novelty of the prints and are very happy if the saving in labour costs is divided between their accountant and themselves. Of course, prints of pre-printed dummy balance sheets and handwritten income statements, are not acceptable for many purposes. But for the taxpayer whose annual financial statements are drawn up mainly to suit the requirements of the taxation authorities, prints are generally satisfactory.

Here is a revolutionary development for accountants in the processing of tax returns. Let us hope their traditionally cautious approach will not prevent them too long from deriving the benefits to be realized.

Recommendations on the Income Tax

Joint Recommendations on the Income Tax Act and Excise Tax Act submitted by The Canadian Bar Association and The Canadian Institute of Chartered Accountants

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A. THE INCOME TAX ACT

1. PAYMENTS BASED ON PRODUCTION OR USE

S. 6(j)

It is recommended that in connection with payments based on production or use, this section be amended to make it clear that capital payments received on the disposal of property are excluded from this section when the purchase price is definite and payable within a reasonable time.

2. DEDUCTIBILITY OF BUSINESS EXPENSES

Secs. 11(1) and 12(1) as amended

Section 12(1) of the Income Tax Act provides that in computing income no deduction shall be made in respect of:

(a) an outlay or expense except to the extent that it was made or incurred by the taxpayer for the purpose of *gaining or producing income* from a property or a business of the taxpayer;

(b) an outlay, loss or replacement of capital, a payment on account of capital . . . .

These provisions (and others as as well) have been interpreted that many expenses necessarily incurred in carrying on the business are not now deductible in computing income for taxation purposes. Having regard to the present high level of taxation in Canada, these disallowances impose a definite hardship. We appreciate the fact that a clear definition of deductible expenses, satisfactory to all taxpayers, is almost impossible to achieve and we believe that greater flexibility can be achieved without seriously impairing the revenue of the Crown and without changing the basic concepts upon which our present Act is founded.

For example, expenditures which, although necessarily incurred for business purposes, are held to be non-deductible in determining business profits under the Income Tax Act include:

(1) legal and other costs including professional fees in connection with the ascertainment of income tax payable on business profits (including appeals from assessments) or in connection with actions brought against the business which do not result in the acquisition of any asset of

enduring value already possessed by the business;

(2) the costs of acquiring or protecting a franchise, or other long term advantage which, though having in fact a life shorter than the life of a business, is not limited to a definite period in the document which gives rise to it.

It is submitted that the principle should be recognized in our Income Tax Act and in the administration thereof that expenditures of the above nature made and incurred for business purposes should be deductible in the determination of business profits for taxation purposes for the year in which they are made or incurred, and that appropriate amendments should be made to the Income Tax Act.

3. DEDUCTION OF INTEREST ON FIXED TERM DEBT ISSUED AT DISCOUNT

S. 11(1)(c) as amended

Under section 11(1)(c) a deduction is permitted of the amount of interest (to the extent that it is reasonable)

(1) upon borrowed money used for the purpose of earning income from a business or property, and

(2) upon money payable for property acquired for the purpose of gaining or producing income therefrom or from a business....

Where bonds or debentures to secure a loan are issued at a discount, i.e. for less than the amount repayable by the borrower, the borrower is allowed no deduction for the amount of the discount despite the fact that it is as much a cost of the loan as is the interest thereon. Further, that part of the discount which is the underwriters' commission is taxable in his hands.

Recommendation: It is recommended that a deduction for such charges as are mentioned above should be allowed in the cases of bonds, debentures and other fixed term debt issued on a basis whereby the same are not convertible into share capital, by amending section 11(1)(c):

> to permit the deduction of discount and/or underwriters' commission on bonds, debentures or other fixed term debt (excluding debt issued on a convertible basis) not exceeding 5% of the face amount of the security.

4. PENSIONS FOR SELF-EMPLOYED

S. 11(1)(i)

This matter has been the subject of a special brief presented by the Canadian Bar Association and the Canadian Institute of Chartered Accountants.

5. CAPITAL ELEMENT IN ANNUITIES

S. 11(1)(k)

Recommendation: It is recommended that the Income Tax Act be amended to provide that only the net amount received under a pension plan or annuity, that is, the amount remaining after deduction of the succession duty payable with respect thereto, should be treated as income of the recipient.

6. INTEREST ON SUCCESSION DUTIES

S. 11(1)(o)

It is recommended that this section be amended by the addition of the words "or interest actually paid on money borrowed for the specific purpose of paying succession duties or inheritance taxes, but not in excess of the interest rate that would be

charged by the government to whom the duties were payable".

7. METHOD OF COMPUTING INCOME
S. 14(1)

Recent jurisprudence appears to have rendered the meaning of section 14(1) obscure, especially as regards "accepted for the purposes of this part". There is also uncertainty regarding the meaning of the words "method for computing income from a business or property".

The reported decisions *Ken Steeves Sales Limited* v. *M.N.R.* and *No. 282* v. *M.N.R.* indicated that some doubt existed as to whether a method of computing income can *ever* be accepted by the Minister in view of his right to reassess. If this doubt is justified the effect of section 14(1) would be nullified and a method of computing income could never be considered adopted and accepted so as to bind either the taxpayer or the Minister in future years.

Recommendation: It is recommended that provisions should be introduced to the effect that:

> a method of computing income is deemed to be accepted for the purpose of section 14(1) if the Minister accepts such method in writing or if the method has not been rejected by the Minister within two years after the receipt of the original assessment for the first year in which the taxpayer adopted that method.

8. LEASE-OPTION AGREEMENTS
S. 18

Under section 18 property which is the subject of a lease-option or similar agreement is deemed to be the property of the lessee, who is therefore disentitled to deduct the rental payments in computing his income but may claim capital cost allowances based on the price of the property fixed by the agreement. This section is intended to prevent the purchaser from, in effect, writing off the real price as rent in a shorter period of time than if he were confined to the capital cost allowances permitted by the regulations. It follows that if the option price fixed by the agreement is in fact not less than the fair market value of the property at the date of the agreement, an inequity results from the allowance to the lessee of smaller annual deductions than the rent which he pays.

Recommendation: It is accordingly recommended that the provisions of section 18 should not apply in the case of real property if the option price fixed by the agreement is not less than the fair market value of the property at the time the agreement is made.

9. HUSBAND AND WIFE
S. 21(2) and (3)

This section disallows the deduction from taxable income the remuneration paid to a wife when she is employed by her husband or vice versa.

Recommendation: It is recommended that the remuneration received by an employed spouse should be deductible and treated as separate income in the employee's hands where the services are actually performed and the compensation is not greater than would be paid to another person for the same services. A similar objection applies to section 21(3).

10. DIVIDEND CREDITS
Secs. 26 and 38

Where the income of a wife is over \$250 but below \$1,000 the excess of

her income over $250 is, in effect, added to the husband's income through a reduction of his marital exemption. If the income of the wife consists of dividends, the 20% tax credit is lost.

Recommendation: It is recommended in such cases that the husband be allowed the 20% credit on that portion of the dividends by which the husband's taxable income is increased.

11. LIMITATION ON DEDUCTION OF SPOUSE
S. 26(2)

At the present time a single person with a dependent has a tax advantage over a married person in that said dependent can earn up to $750 without affecting the personal exemption of the taxpayer supporting the dependent.

Recommendation: That section 26(2) be amended to allow a spouse to earn $750 before affecting the marital exemption of $2,000 allowed to her husband.

12. CHARITABLE DONATIONS MADE BY CORPORATIONS
S. 27(1)(a)

Under section 27(1)(a) gifts made by a person in a taxation year to recognized charities are deductible in computing the taxable income to the amount of 5% of a corporation's and 10% of an individual's income for the year. In the case of a corporation or an individual carrying on business, the contribution is not recognized as an ordinary business expense, however, with the result that the amount thereof is not taken into account in computing the amount of a business loss which may be applied against the profit of the preceding year and the five succeeding years under section 27(1)(e).

In the conditions of today charitable contributions have, in effect, become ordinary business expenses which virtually every person carrying on business finds it necessary to make as a member of the community. Moreover, corporations and businessmen frequently find it necessary to make binding commitments to contribute a certain amount annually for a number of years to charitable bodies with respect to capital campaigns for the expansion of essential community services. It may thus happen that in any year the amount of a taxpayer's charitable contributions are found at the close of that year to exceed the statutory limit and no deduction can be made for the excess in that year or in succeeding years.

Recommendation: It is accordingly recommended that the Act be amended to permit the amount of charitable donations made in any year but not deductible in that year to be deductible in any of the five succeeding years.

13. MEDICAL EXPENSES
S. 27(1)(c)

The medical expense allowance is presumably designed to allow taxpayers a deduction for catastrophic or unduly severe medical expenses which have the effect of reducing income and which are uncontrollable. The section as presently written limits the amounts of expenses deductible and also the drugs which may be included and therefore the deduction allowable in many cases falls short of the original intention of the legislators.

Recommendation: It is accordingly proposed that the present restrictions on the amounts allowable be rescinded.

14. DESIGNATED SURPLUS OF RELATED CORPORATIONS

S. 28(2) et seq.

It is considered that this section and other sections which are concerned with designated surplus go so far that they impose a tax penalty on business transactions which are normal and desirable for ordinary business purposes, particularly where the corporations concerned are subject to the same final beneficial ownership.

15. CREDIT FOR PROVINCIAL CORPORATION INCOME TAXES

S. 40: Regs. Part IV

The announced intention of section 40 was that a company which resided or carried on business in a Province which imposed a corporate income tax should not, merely because of that circumstance, be subject to a greater total amount of taxation, apart from that arising from variations in provincial taxes, than any other company which did not reside or carry on business in the province. The credit under section 40(1)(b) was clearly intended to produce this equalizing result.

Because of the differences between the rules of allocation of a company's income under the Quebec Corporation Tax Act and under Part IV of the Income Tax Regulations, equalization will rarely occur in the case of a company which carries on part of its activities in Quebec and part in some other province or provinces. In many cases, the credit under section 40 will fall far short of the tax imposed by Quebec and, in other cases, the credit will exceed the Quebec tax by a substantial margin. For example, in the case of a manufacturing company, the usual results will be:

(a) a tax credit that falls short of the Quebec tax if the manufacturing facilities are chiefly outside Quebec; and

(b) a tax credit that exceeds the Quebec tax if the manufacturing facilities are chiefly in Quebec.

The situation described is most undesirable and ought to be corrected.

Recommendation: It is accordingly recommended that the Government of Canada take this matter into consideration with a view to finding a basis of agreement with the Government of the Province of Quebec respecting the allocation of the income of a company to the various places where it carries on business in order that there may be no discrimination between companies as above described.

16. AVERAGING INCOMES OF FARMERS AND FISHERMEN

S. 42

Under section 42 the income of a farmer or fisherman may be averaged in five-year blocs in accordance with the requirements set out in this section, whence it follows that if a farmer or fisherman dies before an averaging bloc is completed there is no right to average his income for the period expired to the date of his death.

Recommendation: It is accordingly recommended that section 42 be amended to permit the income of a farmer or fisherman to be averaged for the period commencing with the taxation year immediately following his last averaging period and terminating with the taxation year in which he died.

17. CERTIFICATE BEFORE DISTRIBUTION

S. 52(2)

As section 116(4) provides for ac-

ceptance of security for the payment of taxes, the granting of a certificate by the Minister under section 52(2) should be extended to cover cases where security is given.

Recommendation: It is therefore recommended that section 52(2) be amended to read as follows:

> Every assignee, liquidator, administrator, executor and other like person, other than a trustee in bankruptcy, before distributing any property under his control, shall obtain a certificate from the Minister certifying that taxes, interest or penalties that have been assessed under this Act and are chargeable against or payable out of the property, have been paid or that payment thereof has been secured under section 116(4).

18. LIMITATION ON INTEREST PERIOD

S. 54(6)

It is recommended that section 54(6) be re-enacted with an amendment to provide that interest shall recommence only from 30 days after the day of mailing of the notice of reassessment establishing any additional amount of taxable income instead of 30 days from the day of mailing of the notice of the "original assessment".

19. WHERE PAID-UP CAPITAL INCREASED

S. 81(8)

A strict reading of this section would appear to mean that the conversion of debentures and other liabilities into capital stock with a resulting increase in the paid-up capital would be deemed capitalization of undistributed income. The shareholders would be taxable to the extent of this capitalization. It does not seem reasonable that this should be the case and with the number of convertible debenture issues of the last few years it could be a matter of considerable importance. If such is a proper interpretation of this section it is recommended that a revision be made to add to paragraph (b) of subsection (8) following the word assets "and/or reduced the liabilities".

20. REVOCATION OF ELECTION TO BE TAXED ON 1949 SURPLUS

S. 105

Under this section when a corporate taxpayer elects to pay a tax on its 1949 undistributed income, it becomes liable for any additional tax that may be found payable on assessment.

The computation of undistributed income in many cases goes back as far as 1917 and frequently there are unknown or doubtful items, some of which may be quite material. An example might be where substantial additions are made to the undistributed income arising from surpluses transferred from predecessor companies of which the taxpayer may have had no knowledge.

Because of the possibility of material differences arising in the computation of undistributed income due to unknown factors, the difficulty of adequately determining all the facts of particular transactions after a number of years, the existence of differences of opinion on interpretation of the law, and the possibility of honest errors, a large additional amount of tax may be assessed that the taxpayer is unable or unwilling to pay.

Recommendation: It is, therefore, recommended that the taxpayer be given the right to revoke an election and recover tax already paid under this section where the assessed tax

exceeds the estimated tax by more than a prescribed percentage.

21. TAX-PAID UNDISTRIBUTED INCOME

S. 105(1), (5) and (8)

Where a taxpayer fails to pay any additional tax assessed under section 105(1) within thirty days from the day of mailing the notice of assessment, he is liable to pay the additional tax but can receive no benefit from the payment because subsections (5) and (8) limit the amount on which the tax is deemed to have been paid to 100/15th of the tax paid with the election or within thirty days of the date of mailing the notice of assessment.

In certain cases valid reasons may exist why the additional tax is not paid within the prescribed time.

Recommendation: It is accordingly recommended that with respect to any additional tax actually paid after thirty days from the date of mailing of the notice of assessment, the tax-paid undistributed income should be increased by an appropriate amount in respect of any such additional tax so paid.

22. NON-RESIDENTS' TAX

S. 106

A resident beneficiary of a non-resident estate or trust is not allowed any tax credit in respect of Canadian tax withheld from income received by the estate or trust from Canadian sources.

Recommendation: It is recommended that Canadian beneficiaries be allowed a proportionate part of the Canadian tax withheld from income of the trust or estate in such case, as a payment on account of tax payable, if any, under Part I of the Act.

23. ARM'S LENGTH — IRREBUTTABLE PRESUMPTION

S. 139(5)

Section 139(5) provides that related persons shall be deemed not to deal with each other at arm's length and that it shall be a question of fact whether persons not related to each other were at a particular time dealing with each other at arm's length. It is submitted taxpayers should not be subject to taxation in Canada on the basis of relationships which are conclusively presumed to exist but which in many cases do not in fact exist.

Recommendation: It is recommended that, in place of the irrebuttable presumption that related persons as defined by subsections (5a) to (5d) and (6) of section 139 do not deal with each other at arm's length, the Act should provide that they shall be *presumed* not to deal with each other at arm's length so that the taxpayer may have the opportunity of rebutting the presumption by evidence satisfactory to a court of law.

24. LEASEHOLDS, PATENTS, FRANCHISES, CONCESSIONS, LICENCES

Reg. 1100(1)(b)

Under regulation 1100(1)(b) the capital cost allowance for leasehold property is computed separately in respect of each property and on a straight-line basis, although all of such leasehold property constitutes one class under class 13 of Schedule B. The same is true under regulation 1100(1)(c) of patents, franchises, concessions and licences described in class 14 of Schedule B. Under section 20(1) and regulation 1100(2), however, all of a taxpayer's property of one of the classes described is lumped

together for the purpose of recapturing capital cost allowances and claiming a terminal allowance.

Recommendation: It is recommended that a taxpayer have the right to elect that each item of property described in classes 13 and 14 of Schedule B constitute a separate class so that the recapture and terminal provisions, as well as the percentage deduction provision, *may* apply to each property separately and that, once an election is made, it be binding on the taxpayer and not changeable except with the consent of the Minister.

25. NOTICE OF REASSESSMENT — APPEAL PROCEDURE

The original notice of assessment indicates on the reverse side in small print the procedure which must be adopted if the taxpayer wishes to object to the assessment. The notice of reassessment is more likely to give rise to an objection by the taxpayer. It does not contain such a statement but simply refers to the original notice in a note appearing at the bottom of the reverse side. Neither notice makes any easily seen reference to the objection procedure on its face.

Recommendation: It is recommended that the wording which appears on the reverse side of the original notice of assessment setting out the objection procedure should be repeated in bold print on the face of the notice of reassessment.

It is further recommended that the prescribed form of notice of objection be amended so as to permit signature by the taxpayer or his agent.

26. UTILITY SERVICE EXTENSION COSTS

Such expenses as occur when installing a power line extension or telephone line extension etc. do not fall into any capital asset class as they are not owned by the taxpayer. They are therefore not subject to a depreciation allowance.

In addition, these costs are not allowed as an expense of the year by the taxing authorities.

Recommendation: That some provision be made whereby such costs can be amortized or expensed.

B. THE EXCISE TAX ACT

27. SALES TAX

The report of the committee appointed by the Minister of Finance, to consider and review certain matters pertaining to sales and excise tax, advocates the definition of a sales tax price and provision of reasonable means of legal content of decisions of the administration with respect to matters of fact and matters of law. This committee expresses the hope that these recommendations will be implemented by appropriate legislation.

New Office Equipment and Business Machines

The Canadian Chartered Accountant has recently received information on the following new office equipment and business machines:

ELECTRONIC ACCOUNTING

The new *IBM Electric Typewriter* with Electronic Tabulation, manufactured by International Business Machines Ltd., eliminates time consuming tabulating adjustments, it is claimed, no matter how many different types of forms are placed in the machine. The electronic device of the typewriter "reads" business forms specially printed with vertical lines of electrically-conducive ink, and automatically positions the typewriter carriage.

The *IBM 305 RAMAC* (Random Access Memory Accounting Machine), manufactured by the same company, is a complete data processing machine which is built around a disk memory unit having a storage of 5,000,000 digits. This unit consists of 50 magnetic metal disks arranged in a vertical stack with data recorded on or read from each side of the disks by a rapidly moving arm. RAMAC also has arithmetical and logical processing ability, punched card input, and both punched card and printed output. The company has also produced the *RAM 650,* one of the first of IBM's line of machines designed for high-volume, "in-line" processing of business data. Instead of accumulating data to be processed in batches, each transaction is processed as it happens and, at the same time, every related record in RAM is adjusted. This machine is a basic magnetic drum data processing machine with an IBM 355 Random Access Memory (RAM). A new link in industrial data handling is IBM's Automatic Production Recording System, consisting of standardized components designed to collect, correlate, store and record production data automatically from various measuring instruments. A functional input component of the APR system is the console control unit. This unit permits the manual introduction of production line data into the system. The console may contain an automatic IBM electric typewriter, a commutator clock, a console control unit and various other components such as counter panels.

A new, low-cost mobile, electronic computer, whose wide range of applications includes many of special interest to industry in general, has been introduced on the market by The McBee Company Limited.

Called the *LGP-30,* the desk-size computer has a memory capacity of 4,096 words, can be operated by non-technical personnel. It is a self-cooled, serial, single address, fixed point, binary stored digital computer. Requiring no special installation, it operates from a wall outlet.

ADDING MACHINES

A new model *Ten Key* electric adding machine featuring a newly-designed keyboard, greater operating simplicity, two-colour ribbon, automatic spacing for tear off after totals, and new high operating speed has been marketed by Burroughs Corporation throughout Canada.

The new model is distinguished by unusually high speed and a "Balance Touch" keyboard described as "a carefully designed combination of proper key positioning and balanced key feel". Distances between outlying keys and the home-key position have been re-engineered to make them as nearly equal as possible.

CALCULATORS

Silver Bells Ltd., 600-16th St., Oakland, Calif., are the distributors for the *Controller,* a small circular calculator that gives the performance of the 10-inch slide rule but measures only 3 inches in diameter. Of aluminum construction, it weighs one ounce including its vinyl carrying case. An accompanying 12-page booklet of instructions shows how it may be used for multiplication, division, exchange rates, currency calculations, percentages, etc.

BY LAWRENCE G. MACPHERSON, F.C.A.

The Director of Research, C.I.C.A.

Accounting Research

The general suitability of the standard bank confirmation forms has been demonstrated in their use by practising members for the past 12 years. In most instances, they are used without modification, which presumably was the result desired when they were introduced. The form could not serve every possible circumstance, and occasionally an accountant has required banking information not covered by it. In addition, some firms have preferred a change in the form for their own purposes. These situations have been met in various ways, by the use of supplementary letters, by requests typed on the printed form, or by additional printing on the form.

The standard form does not allow much space for additional typed requests, and no space is specifically designated for that purpose. Whether it should be provided is a question of the extent of the need, since unusual circumstances can be met satisfactorily by attaching a special letter.

The private printing of additional requests on the form destroys the significance of the printed approval by the Canadian Bankers Association and the C.I.C.A., unless the extra requests are clearly indicated as private inserts. In the absence of this indication, any variation from the standard form would call for a deletion of the words signifying official approval.

In this month's research article T. A. M. Hutchison, a member of the Committee on Accounting and Auditing Research and a recognized authority on bank affairs, considers some suggestions concerning the bank confirmation forms. His views will interest all accountants who use the standard form, especially those who have made suggestions for its revision. Further comments will be welcomed by Mr. Hutchison and by the committee as a whole.

One member has suggested that the form might include a request to the bank to supply copies of all deposit slips for a specific period. This is not dealt with in the article, as the extent of the practice as an audit procedure is not clear, and in any case a bank could handle a separate request more conveniently.

The value of duplicate deposit slips, whether obtained from the client or the bank, may be questioned in view of the fact that the banks in many cases do not compare the amounts of individual cheques with the deposit slip. The research department would like to know more about the extent of the practice of comparing the details of cash receipts with duplicate deposit slips. It seems to vary a great deal, but this is merely a vague impression which may not be clarified until a survey of practice has been made. Meanwhile, would any practising members care to volunteer a report on their own use of this technique, or their opinion of its usefulness?

THE STANDARD BANK CONFIRMATION FORM

T. A. M. Hutchison, F.C.A.

The standard bank confirmation form which can be purchased from the Canadian Institute of Chartered Accountants was developed over ten years ago by the members at that time of the Committee on Accounting and Auditing Research. The original request for a standard form arose from consultations between the Government of Canada and the chartered banks, which took place during the war years to see if anything could be done to cut down the detail work of the banks in the light of the prevailing shortage of manpower. In order to develop a suitable form, a joint committee was set up composed of members of the Canadian Bankers Association and the C.I.C.A. Committee on Accounting and Auditing Research. The form, prepared by the latter, was submitted to the former for their approval and was thus able to carry the notation "approved by The Canadian Bankers Association and The Canadian Institute of Chartered Accountants", which ensured the cooperation of the banks in completing it.

From time to time there have been suggestions for changes in the existing form, mainly to obtain additional information which practising members feel would be helpful in conducting audit engagements. Some have said that the form should show the rate of interest on any bank loan, that bank accounts closed out during a year should be listed, that deposits for the first few days following the financial year end should be listed and that the last section of the form should be divided so as to segregate the space for securities held for safekeeping. No doubt other suggestions could be made to meet particular requirements of audit engagements.

It must be remembered that the completion of bank confirmation forms represents a very considerable task for the banks. Particularly in the period following December 31, when many companies end their financial year, the banks are literally deluged with bank confirmation requests from auditors.

Consequently in considering any change or amplification of the bank confirmation form, we must bear in mind that we should not ask the banks to do anything more than is really necessary to carry out our audit work in a proper manner.

It would appear that the rate of interest charged by a bank on any bank loan can be determined quite easily by the auditor by relating the interest charge for a month to the amounts of the bank loans. Presumably if the auditor wishes to satisfy himself that the rate of interest being charged is proper, he can refer the rate so developed to the responsible officer in the company and ascertain that this is the rate agreed upon with the bank. The rate of interest is indicated for balances on deposit with the bank but it would seem that the request for this information might be eliminated from the form since it is not required in most cases.

The standard form used in Canada calls for debit and credit balances (overdrafts and deposits respectively) to be reported in section 1, with loans reported in section 2. Occasionally, however, overdrafts are reported under loans in section 2.

The standard form approved by the American Institute of Accountants and the National Association of Bank Auditors and Controllers for use in the United States calls for reporting credit balances only in section 1, so that by implication all borrowings would be reported in section 2. It would appear that something could be gained either by reporting all borrowings in one section as in the U.S. form or else by clarifying section 2 of the Canadian form so as to specifically exclude borrowings by way of overdrafts.

There would appear to be some merit in requesting a list of accounts that have been closed out during a year since the auditor must be sure that he has knowledge of all bank accounts operated by the company. It might be possible to open a bank account, deposit therein cheques received made out in the name of the company, and subsequently withdraw the funds by cheque without making any record of the transactions in the books of the company concerned. At the same time it must be remembered that, particularly in the larger branches of a bank, it will be a burdensome task for the bank to ascertain that it has reported all accounts of a customer closed out during the year.

Information as to deposits made in the first few days following the financial year end may well be required with respect to the principal bank accounts of a company, but with payroll and transfer bank accounts the information would not seem to be of sufficient importance to the auditor to ask the banks in every instance to list deposits made for several days. Actually the need for requesting a list of deposits for the first few days could often be obviated if the auditor adopted a practice, which is sound from an audit viewpoint, of requesting the bank to deliver direct to him the bank statements and cheques for the month or period following the financial year end so that the principal banking transactions in the early part of the ensuing year can be investigated. If the banks are to be asked for a list of deposits for the first few days of the succeeding year, this should only be done where the information is needed, say on the principal bank accounts. A specific request should be made to the bank for this information.

The suggestion that a special space should be provided to list securities held for safekeeping would be quite reasonable except that the size of the form and the material now set out in it would make it difficult to add additional sections, particularly if the suggestion set out in the next paragraph were adopted.

In a good many instances the auditor does not need to request certain information and in other instances he may wish to make a request for specific information which is not dealt with in any other way on the form. It might be worthwhile to raise a further section in the bank confirmation form which would be so headed as to indicate that no reply was required unless a specific question was asked. The auditor would then complete the section if he wanted information. For instance, he might ask for a list of deposits with dates and amounts for the first five business days of the month.

A further proposal which might meet some of the space problems is to shorten section 2 in which loans are reported; to provide a separate

section for particulars of safekeeping securities; to combine the present sections 3 and 4 omitting, of course, particulars of safekeeping securities; to include as a last section a box for requesting specific information.

If changes in our amplification of the bank confirmation form are desirable at this time, they can only be made effective with the cooperation of the Canadian chartered banks. If this is to be done, it will no doubt be necessary to enlist the cooperation of The Canadian Bankers Association for working out amendments to the existing form. We should bear in mind that by and large the standard bank confirmation form has served satisfactorily since its adoption in 1946 and that, while we may well ask for changes in presentation, we should not request more information where the work involved will be burdensome unless there is a genuine need.

TRUE SERVICE AND ACCOMPLISHMENT

Whatever may be the economic success and public recognition of a profession, whatever may be the growth of its membership, however rigid may be its regulations for admission and practice, its true service and its accomplishment will depend on the quality of preparation of its members . . . . However well we regard the accomplishments and progresses of the past, there is always more that can be done, better results to be sought, and new truths and methods to be discovered and developed.

We should always remember that accountancy is a profession in which only the highest levels of integrity and character are adequate. It is the responsibility of the teacher, therefore, to train the student not only in good technical principles and procedures, but in the fundamentals of attitude and conduct as well. Only if he is so grounded will he be prepared to meet his obligation to the public and his profession not merely as a good technician, but even more importantly, as a good person.

— From an address by Lloyd Morey, president, University of Illinois, to the American Accounting Association, September 1954.

BY GEOFFREY H. WARD, C.A.

Practitioners Forum

Processing Tax Returns

Many public accounting firms have found that income tax work is the most important single technical area in which they serve their clients. In *The Journal of Accountancy*, June 1956, Max Myers wrote a letter to the editor making a good case for the profession's obligation to handle "small returns". Certainly in the smaller centres personal income tax matters form a significant part of most practices.

This situation poses a problem to partners responsible for organizing their firm's tax work. The job must be done efficiently, accurately and on time, and clients must get the full benefit of the knowledge of the partners. To expedite this kind of service, this month's column will examine office organization of procedures, forms and routines for volume preparation of tax returns, namely: T-1's and T-2's.

Several firms were asked questions on their approach to this problem. Do they use forms, check lists, questionnaires? Do they have a formal routine? What levels of staff prepare, check and review the returns?

Timing

In view of the penalties for late filing and the nightmare of a last-minute rush, advance planning is obviously essential. One panel member reports as follows:

"We accept the responsibility of seeing that our clients' returns are filed on or before the due date. For this purpose, we keep lists on working papers. T-1 lists are prepared alphabetically and start with the list of returns filed for the year before. To this we add the names of new clients.

"The list has space for the initial of the staff member responsible for the preparation of the return, the date the return is completed, the date sent to the client for signature, the date filed and comments. If the client files the return himself or if he undertakes to prepare it himself, this is noted.

"Periodically during the T-1 season, the list is reviewed by a partner and pertinent queries are raised with those charged with the preparation of returns."

An interesting angle is reported too. "We have found that if we attempt to get the information we need from the taxpayer around the beginning of the year, i.e. January or February, there is usually a long delay before it is forwarded to us. Also, information to be supported by T3, T4 and T5 slips is not always available until the beginning of March. As a result we usually delay requesting information until the end of March or the beginning of April. By then the client himself is usually getting concerned about filing his return so that it is easier to extract the information."

Letters — Inquiry

Here is a sample of a brief form letter used by one firm:

"We are enclosing herewith an income tax information sheet to be completed for Mr. –. This information is required in connection with the filing of his 19– income tax return.

"Please record the necessary information and return same to us, together with any medical or donation receipts that may apply.

"This information should be in our hands not later than ––.

"Thank you for your prompt cooperation in this matter."

While sceptics may question the client's ability to complete the information sheet, many firms follow this routine successfully.

Collecting Data – T-1's

Many accountants use the T-1 form as a guide. However, some prefer special questionnaires. Here is a sample of one to be completed by the accountant:

"CLIENT ———————— DATE ——

A. Obtain details of all income
Including T3, T4, and T5 slips, where available.
(1) Bonus
Pension
Salaries
Subsistence allowance
Value of free board and lodging
Wages
(2) Old age security pension
(3) Net profit from business,
Profession or commissions
(*State type and attach statement*)
(4) Directors fees. Executors fees
(5) Farming or fishing
(6) Investments
a. Dividends
b. Mortgage interest
c. Bond interest
d. Bank interest
e. Annuities
f. Estates or trusts
g. Royalties
h. Alimony
(7) Rents
(8) Foreign income

B. Deductions from income
(1) Alimony paid
Automobile or other expenses
Pension plan contributions
Union or like dues
(2) Personal exemptions
Basic exemptions
If over 65 – year of birth
Dependent exemptions (*List dependents – with details of their incomes*)
a. Spouse
b. Children (*If over 21 state school*)
c. Housekeeper
d. Brothers or sisters
e. Parents (*State amount of support given*)
f. Clergyman
(3) Charitable donations
Medical expenses (*Check prior year for carry over*)
(4) Business losses carried forward
(5) Deductions from investment income
Dividends (*Depletion and carrying charges*)
Carrying charges (*To be pro-rated between dividend income from taxable Canadian corporations and other investment income*)
Investment counsel fees (50%)
(6) Rents (*Expenses of properties including depreciation*)

C. Calculation of Tax
(1) Calculate tax based on current rates (*Attach calculation*)
Income tax
Old age security tax
Surtax
(2) Deduct 20% of net dividends from taxable Canadian corporations
(3) Deduct foreign taxes paid or proportion thereof.
(4) Instalment or other payments

D. General
(1) Examine previous year's return, compare with current year, make notes of any changes in source of income or type of deduction.
(2) Examine prior year's assessments.
(3) Note any gifts made during the year of more than $1,000."

Routines for Returns

A practitioner writes that his file of clients includes:

a. Cards, in alphabetical order, showing name of client, address, telephone number, fiscal year end.
b. Cards, in chronological order of due dates of returns, showing fiscal year ends, corporate and other returns required. Under April the T-1 card shows a list of all these returns for which we are responsible.

He describes his routines as follows:

1. Each year five copies of this list are typed. The initial of the person responsible for the preparation of each return is shown.
2. The person preparing the return then draws the necessary files and writes to the client requesting any information which we have not already on hand. No standard letter is used. The information requested is based on the previous year's return but a general query as to other income or expense is always included.
3. At the same time as the letter goes out, the T-1 tax questionnaire is filled in as far as possible and placed in the client's file.
4. When the information requested has been received the returns and schedules thereto are prepared. Notes are made in the file of any comments which should be passed on to the client.
5. The arithmetic on the returns is then checked by another member of the staff.
6. The completed return then goes to one of the partners for a thorough review. A letter is dictated to the client and the return is approved for typing.
7. Three copies of the returns are typed, one each for the Income Tax Department, the client and our files. As typing instructions for income tax returns are usually very brief they are written on the top of the pencil draft of the return.
8. The office copy of the typed return is then called, checked and added. A rubber stamp, with space for initials, is used to record these steps.
9. The partner sees that the checking has all been initialled, marks the return off his master list, signs the letter and sends on the bad news to the taxpayer.

Another practitioner reports that he follows this procedure:

1. A questionnaire is mailed to the client along with a form letter.
2. On receipt of the questionnaire it is reviewed and completed by the member of staff handling that account.
3. It is then scrutinized by a supervisor.
4. The income tax return is prepared in pencil, usually by junior members of the staff.
5. The prepared return is checked for calculation and disposition of income, etc., usually by intermediate members of the staff.
6. The returns are then typed and checked for correctness of typing.
7. Documents are attached.
8. Completed forms are scrutinized by supervisor.
9. Forms are mailed with form letter to taxpayer.

Letters of Transmittal

Here is a sample:

"We have now completed your 195– income tax return and enclose same herewith. Your total tax

amounts to $....... However, according to our records, you have already paid the Department $.......

"It will therefore be necessary for you to sign the enclosed forms and forward them together with a cheque in the amount of $...... to the District Taxation Office at ....

"It is necessary that these forms be in the mail not later than .... in order to avoid penalties."

In some cases a caution is included to clarify the client's responsibility for statements in the returns. This might read as follows: "The statements made in the returns and the attached schedules have been compiled by us from information supplied by you and obtained from the records of the company. As you are required to certify that you have examined the returns and that they are true, correct and complete, we suggest that you review them carefully to make sure that there is nothing contained therein to which you would be unable to certify."

(*This commentary will be concluded in the May column.*)

AN INVITATION TO PARTICIPATE IN PRACTITIONERS' FORUM

The profession generally agrees that the required extent of testing of transactions varies with the adequacy of the system of internal control. However, the practical application of this principle confronts the auditor of a small business with a real problem.

To quote the editor of *The Virginia Accountant*: "If internal control is adequate, we can limit our examination to well selected tests. If internal control is not adequate, how far must the tests proceed? Or suppose no internal control exists, must a 100% verification be made of every transaction? What about the small business operated by one officer-stockholder and one office clerk – all of the accounting functions being performed by the officer? This condition, or one closely approximating it, frequently occurs. Is this a case of no internal control, or perfect internal control? Is the auditor required to examine every transaction before rendering an opinion?"

If you will send in your views on the solution to this problem, the editor will be happy to prepare a column discussing the subject.

BY MELVILLE PIERCE, B.A., LL.B.

The Tax Review

Instalment Sales

Mr. Justice Thorson, the President of the Exchequer Court of Canada, has pronounced another of his weighty judgments on accounting for tax purposes, this time on the question of instalment sales. In the judgment delivered on December 28 last in the case of *Publishers Guild of Canada Ltd.* v. *Minister of National Revenue,* the learned President has held that, under the Income War Tax Act at any rate, the so-called instalment sales method of accounting was permissible for taxation purposes if the circumstances were appropriate. Before going into the case, however, it may be as well to re-examine a few earlier decisions which bear on the subject.

In *Kent* v. *MNR,* a Tax Appeal Board composed of two members (the present chairman and Mr. Monet) rejected the instalment sales method. In that case a vendor of musical instruments claimed that he was entitled to report his income from sales for the 1948 taxation year as being the estimated profit portion of instalments actually received in cash in that year. The Minister opposed that claim, relying very largely on a passage from Professor Smails' book, "Accounting Principles and Practice" where he states (p. 412):

> The reality of the matter is . . . . that instalment selling poses a problem of finance, not a problem in the accountant's measurement of income. Income is realized as fully when an asset is sold for a promise of cash as when it is sold for cash down.

Shortly afterwards, Mr. Fordham, at that time the third and last member of the Income Tax Appeal Board as it was then constituted, was called on to consider the same question in the case of *90* v. *MNR,* and it was his judgment in this appeal that has now been affirmed by Thorson P. In this case the taxpayer was in the business of selling magazine subscriptions by door-to-door soliciting. The contracts into which it entered with customers called for the delivery to the latter of three magazines and three books for a total price of $29.90, of which $3 was payable in cash, a further $2.90 on delivery of the books, and the balance of $24.00 in 24 weekly instalments. A very high proportion of customers defaulted on their instalment payments and although the books were subject to being repossessed on default such action was never taken as the books had negligible re-sale value. Neither were the contracts acceptable for trade discounting, and collection losses were heavy.

In its 1946 taxation year the company reported a net profit of $16,000 only and "unrealized gross profit" of $60,000, this last being the estimated profit portion of instalments due following 1946 on contracts made in that year. The Minister, after having first indicated to the taxpayer that this method would be acceptable, changed his mind and assessed the

taxpayer to tax in 1946 on the "unrealized gross profit" as well as on the profit acknowledged by the taxpayer. The Minister's view was apparently that even under the Income War Tax Act the income from a business must be computed in accordance with the accounting principle described by Professor Smails and quoted above, i.e. that all amounts received and receivable from a sale made in a year must be entered in the accounts for that year subject only to a deduction in that year for expected losses in subsequent years. Mr. Fordham met this contention head-on by rejecting its major premise and asserting that in the circumstances of this case the instalment method of income reporting was the appropriate method.

The appeal from Mr. Fordham's decision has now been rejected by Mr. Justice Thorson, and for much the same reasons. We quote one passage therefrom:

> "But the court must not abdicate to accountants the function of determining the income tax liability of a taxpayer. That must be decided by the court in conformity with the governing income tax law. It is an established principle of such law in this court that there is a statutory presumption of validity in favour of an income tax assessment until it is shown to be erroneous and that the onus of doing so lies on the taxpayer attacking it. But while the court must be mindful of this principle it must in its efforts to apply the law objectively keep a watchful eye on arbitrary assumptions on the part of the tax authority such as, for example, that it is within its competence to permit or refuse any particular system of accounting and that its decision in this matter is conclusive. I cannot express too strongly the opinion of this court that, in the absence of statutory provision to the contrary, the validity of any particular system of accounting does not depend on whether the Department of National Revenue permits or refuses its use. What the court is concerned with is the taxpayer's income tax liability. Thus the prime consideration is, in the first place, whether it is appropriate to the business to which it is applied and tells the truth about the taxpayer's income position and, if that condition is satisfied, whether there is any prohibition in the governing income tax law against its use. If the law does not prohibit the use of a particular system of accounting then the opinion of accountancy experts that it is an accepted system and is appropriate to the taxpayer's business and most nearly accurately reflects his income position should prevail with the court if the reasons for the opinion commend themselves to it.

The question remains whether the instalment system, as approved in the circumstances of this case by Thorson P., remains a permissible method under the Income Tax Act passed in 1948, having regard to the amendments which have been effected in the years since. The Income War Tax Act, it will be recalled, defined income as "profits and gains *received*" and Mr. Justice Thorson attached considerable significance in his judgment to the presence in the definition of the italicized word. The 1948 Act, however, dropped the word "received" and defined the income that is subject to tax merely as being the taxpayer's "income for the year", including income from all businesses. Did this effect any change in the law?

There are those in whose opinion the changed definition did effect a change in the law, and make the earnings system of income reporting mandatory for all businesses and thus, perhaps, rule out the instalment system. In view of the language of s. 14(1) of the Act this view is highly

debatable, but at all events the question, so far at least as the instalment sales method is concerned, was resolved by the enactment in 1953 of the special provisions under the heading "Special Reserves". By these amendments it is now the law that in computing annual business income for tax purposes all unearned receipts must be included and, in addition, all receivables stemming from sales made in the year *unless the method adopted by the taxpayer for computing income from the business and accepted for the purpose of this Part does not require him to include any amount receivable in computing his income for a taxation year unless it has been received in the year.* (*s. 85B(1)(b)*)

In the judgment from which we have just quoted a lengthy passage, the learned President of the Exchequer Court animadverted with some indignation at the suggestion of a right in the Department of National Revenue to reject an accounting system selected by a taxpayer which was not prohibited by the terms of the Act itself. Under the present Act the taxpayer has the right to choose the accounting system he wishes and, if it meets the test set out by Mr. Justice Thorson, the Minister cannot reject a computation of taxable income based on that system. But, and this is of major practical significance, under the law a taxpayer cannot change his accounting system without the Minister's concurrence. And since it would appear that few if any taxpayers have adopted the instalment method of reporting they are now effectively prevented from taking advantage of this judgment unless the Minister is willing that they should. Those commencing new businesses, however, are under no such difficulty.

EARLY TAXATION

The Romans had the right ideas of taxing. For a start, they rated a tax-gatherer higher than an admiral of their fleet; priests refused to pay taxes before the year 558. We know of the ground-tenth instituted by Hiero and Carthage in Sicily, but when the Biblical writer spoke of "a decree went forth from Caesar Augustus that all the world should be taxed", he was referring to a census. All the world was taxed by Rome, which itself found that the habit of dedicating one-tenth of the citizens' substance produced such a surplus that twice every month public entertainments on the proceeds were held in the Forum Boarium in Rome. A similar thought would be of a budget surplus in the 20th century financing the Arsenal Football Club in Trafalgar Square. Britain had to pay Rome the *Tributum* (property tax), the *Annona* (grain for the army), and the *Vicesima heridatum et legatum* (a 5% legacy duty for the franchise). Seneca lent money to Britain, probably at high rates of interest, to pay the taxes, and his calling it in was one of the reasons for Boudicca's revolt; and this in spite of a contemporary writer's remark: "Taxes and other burdens they bear cheerfully if they are spared actual outrage".

—*Taxation*, December 22, 1956

BY PETER C. BRIANT, B.COM., C.A.

Current Reading

MAGAZINE ARTICLES

ACCOUNTING

"Lifo as a Spur to Inflation – The Recent Experience of Copper," by Waino W. Suojanen. *The Accounting Review, January,* 1957, pp. 42-50.

It is frequently claimed that by eliminating speculative profits from the income statement, the *Lifo* method of inventory valuation acts as a counter-cyclical, stabilizing force in the economy. This would probably be true if businessmen were solely concerned with maintaining a balanced relationship between production and sales. But data gathered by Professor Suojanen, of the University of California, with respect to the copper industry seems to indicate that inventory management policies are now governed by more artificial relationships stemming from income tax considerations. The end result, he says, may well be a situation that accents, rather than mitigates, business fluctuations through the creation of inflationary pressures that would otherwise be absent. In consequence, the expansion and contraction stages of the inventory cycle may be exaggerated, and inventory investment may become an even more volatile component of gross private capital formation than it has been in the past.

The data for the copper industry in 1955, "a year in which demand far outstripped supply", reveals that stocks were short by 90,000 tons at the year end. Of the total shortage, one-third was required to meet the *Lifo* base stock needs of copper producers and fabricators. In many firms, inventories built and recorded at 1945 prices as low as 12c a unit had been reduced materially in 1955, and profits for income tax purposes would have had to reflect the spread between this low price and the much higher current price of fabricated products. The resulting inflationary pressure was further accentuated by the fact that most large producers and fabricators closed their books on the same date. A bunched demand for the commodity therefore developed to meet an artificial rather than a real need of the economy. To this extent, he concludes, the present version of *Lifo* in the copper industry can hardly be considered as one of the anti-inflationary or counter-cyclical tools of the policy maker.

From the viewpoint of the copper industry itself, it would appear from his testimony that continued adherence to *Lifo* can only spell disaster:

> Once technology has been developed to the point that large-scale substitution of aluminum for copper has occurred, the *Lifo* fetish will be nailed to the mast along with over-capacity of the copper producing industry . . . .

An interesting comment, in the light of the arguments, is the *Anaconda* case.

"An Executive Looks at Accountancy" by Oswald W. Knauth. *The*

Journal of Accountancy, January 1957, pp. 29-32.

Mr. Knauth, who has had a varied career as business executive, government official, teacher and author, views sympathetically the accountant of today attempting to reconcile principles rooted in the past with the needs of an increasingly dynamic and complex economy. The accountant, he states, is "caught in the dilemma of deciding whether it is more useful to maintain uniform standards under changed conditions or to adapt new methods to new conditions, thus sacrificing apparent continuity".

After questioning the validity of some time-honoured concepts in the face of such developments as the sale and lease-back, increasing research expenditures, accelerated depreciation and inflation, he makes some constructive suggestions:

1. Reports should be in round figures.
2. Several estimates might be given, depending on various assumptions.
3. Quarterly or semi-annual reports should especially be in round figures.
4. Costs should be divided between "necessary" and "voluntary": those allocated to the current year, and those for future expansion or technical improvement.
5. For their own protection, accountants should endeavour to break down the generally accepted notion of infallibility which is accorded them.
6. Inter-company and inter-industry comparisons are so arbitrary as to be not only meaningless but dangerous.
7. The public should be educated to the fact that financial reports are based on estimates, and the nature and degree of accuracy of these estimates should be explained and emphasized.

AUDITING

"The Independent Auditor and Internal Control" by Gilbert R. Byrne. *The Journal of Accountancy,* January 1954, pp. 41-46.

Mr. Byrne, an American practitioner, calls for an official clarification of the pronouncements on internal control, to delineate more precisely the responsibility of the independent auditor for its investigation and evaluation. At present, he says, independent auditors plead only limited responsibility for fraud resulting from outright defalcations. Yet they continue to perform exhaustive investigations of internal check, giving less apparent attention to internal accounting control. The investigation of the latter is, in his opinion, of far greater importance because these are the principal controls contributing to fairness of presentation of financial statements, which is the auditor's prime repsonsibility.

The crux of the matter is that while the accounting profession has long recognized its responsibility for investigating and evaluating internal control, and amending its audit programs on the results of such a review, it has made no clear-cut attempt to distinguish between internal administrative control, internal accounting control and internal check.

The first, according to Mr. Byrne, refers to measures adopted to promote operational and administrative efficiencies. Here, he says, the auditor has no responsibility for investigation and evaluation, the audit program being affected by its pres-

ence or absence to a minor degree only. Internal accounting controls, on the other hand, "are designed to bring about the accurate and suitable recording and summarization of authorized financial transactions". Finally, internal check refers to "those accounting procedures or statistical or physical or other controls which *safeguard assets* against defalcations or other similar irregularities". To illustrate:

> The requirements of internal accounting control . . . . are satisfied when the signer of a cheque has before him written evidence that the payments liquidate liabilities recorded by means of approved vouchers and that the data on the cheques have been compared with the voucher, and then cancels the request for payment by appropriate means. But internal check requires that the signer be independent of persons who prepare vouchers for approval, persons who approve vouchers for payment, and those persons who prepare checks . . . .

"Auditing Electronic Records" by F. Kaufman and Leo A. Schmidt. *The Accounting Review,* January 1957, pp. 33-41.

This article is so packed with technical information that it is impossible to do it justice within a brief compass. For auditors already engaged in auditing electronic records, or for those with a special interest in the field, nothing but a reading of the original can possibly suffice. In the authors' view, an interest in electronic equipment cannot be so limited. Within a space of 10 years, they assert, a knowledge of the techniques of electronics will have to be a part of the standard equipment of every first-rate auditor.

With this thought in mind, Kaufman and Schmidt present a preview of some of the things they think can already be listed as facets of the new auditing knowledge.

Developing their discussion around underlying changes in internal control, source data, ledger records, files, and audit trail (conditions they believe will still exist even in a fully electronic office), they advise their readers as follows:

1. Plan audits to integrate your "interference" with normal operations.
2. Do more forward checking.
3. Concern yourselves with controls over programs.
4. Develop a familiarity with the functional capabilities of electronic equipment.

MANAGEMENT

"Long-Range Planning for Company Growth" by William E. Hill and Charles H. Granger. *The Management Review,* December 1956, pp. 1081-1092.

"Organization for Long-Range Planning" by H. Edward Wrapp. *Harvard Business Review,* January-February 1957, pp. 37-47.

"Long-range planning is that activity in a company which sets long-term goals for the firm and then proceeds to formulate specific plans for attaining these goals." From this definition, the close relationship between planning and budgetting can be perceived. But, as presently conceived, long-range planning embraces far more than mere projections of capital expansion and cash flows. Product planning, product diversification, marketing, research, personnel and industrial relations, and economic forecasting all centre into today's picture. It therefore behooves all finance executives to familiarize themselves with problems in these fields if this

area of business activity is not to be forfeited by default to other executives, economists and management consultants.

Increasing competition in product markets; greater research commitments; more complex management problems; heightened management responsibility to stockholders, employees and society; and technical and social changes in industry are five good reasons listed by Hill and Granger why long-range planning is becoming a more active centre of management attention. To these, Professor Wrapp would add the favourable reaction of financial analysts to those situations where management has evidenced some attention to forecasting the scope of future growth, tending to the development of a strong "follow the leader influence".

Whatever the reason, this subject is becoming of such increasing practical importance that neither of these articles should be overlooked.

BOOK REVIEWS

Oil Accounting: Principles of Oil Exploration and Production in Canada, by Robert E. Waller, C.A.; pub. for Can. Inst. of Chartered Accts. by University of Toronto Press, 1956; pp. 99; price $5.50.

The oil industry in Western Canada, which has become an important factor in Canada's development in the postwar period, actually had its beginnings during the 1920's and 1930's in the discovery and development of the Turner Valley field. The majority of companies operating at that time were the small promotional-type, and the accounting procedures they evolved were rather haphazard in many ways. The increased interest in the exploration possibilities of Western Canada, which eventually resulted in the discovery of the Redwater and Leduc oil fields in 1947, saw the influx of numerous United States oil companies as well as the rise of many new Canadian independents. The American companies brought with them accounting policies and procedures which were considerably influenced by the provisions of the U.S. tax law. The Canadian independent companies, while partially influenced by U.S. accounting procedures, have been affected, to a large extent, by Canadian income tax law. The result is that at the present time accounting policies followed by the oil industry in Western Canada are a mixture of these three strains.

Mr. Waller has set out in his book a comprehensive review of these various policies and procedures. He has avoided indicating the "correct" procedure, having recognized that at the present stage of development there is none. However, he has done an excellent job in setting out the problems and the ways that different companies have solved them, together with his opinion as to which procedure best discloses the operating results. His book is a timely addition to the literature on accounting for Canadian industry.

J. R. HARDIE, C.A.,
Calgary, Alberta.

BOOKS RECEIVED

"Consolidated and Other Group Accounts," by Sir Thomas B. Holson, M.B.E., M.A., F.C.A.; Gee & Co. (Pub.) Ltd., London; pp. 154; 25/-.

"Integrated Data Processing for Every Office," by H. John Ross; Office Research Institute, Miami, Florida; pp. 80; $2.00.

BY J. E. SMYTH, F.C.A.

Associate Professor,
Queen's University

Students Department

THE QUESTION CORNER

A company chooses to defer a portion of its income because its products are sold under a warranty agreement. The allocation is then taken into income over the life of the warranty agreement. This appears to be conservative practice in that the revenue is left to be matched with the expense.

Let us now assume that the Income Tax Department does not allow this deferment of income to be left out of taxable income. Is the company justified in deferring the income tax applicable to the deferred income over to the period into which the income finally finds its way, or would conservative accounting procedure require the tax to be all charged against current income?

(*Submitted by J.R.R., a third year student in Toronto.*)

Editor's Reply

There is some disagreement among accountants about the desirability of allocating income tax expense between income periods. According to the theory of matching revenues and expenses, the income tax payable for the current year may be allocated in part to future years. A good deal seems to depend, however, upon what one's attitude is towards income tax, as a charge against revenue. Those who hold that there is an essential relationship between business income and taxable income are more likely to want to allocate the income tax; those who see income tax as a government levy determined by arbitrary rules, not necessarily related to the measurement of business income, are more likely to favour "letting the chips fall where they may" and recording income tax expense for the current year at the full amount payable.

In its *Restatement and Revision of Accounting Research Bulletins,* Chapter 10, the Committee on Accounting Procedure of the American Institute of Accountants has written in part:

> Income taxes are an expense that should be allocated, when necessary and practicable, to income and other accounts, as other expenses are allocated. What the income statement should reflect under this head, as under any other head, is the expense properly allocable to the income included in the income statement for the year.

The Committee on Accounting and Auditing Research of the Canadian Institute of Chartered Accountants has considered the advisability of allocating income tax in relation to a reduction of current income taxes caused by claiming capital cost allowances in excess of recorded depreciation. In its Bulletin No. 10 it stated:

> Accounting measurements of income recognize the principle of matching costs and revenues. This principle embraces

the rule that expenses incurred in earning revenues are properly chargeable against the income of the period in which the related revenue is reflected in the accounts. The matching process is not concerned with the time at which the expense becomes payable. Instead, it is a process of allocating expense to the period in which the associated revenue is recognized. Canadian corporate income taxes are of such a character that, in appropriate circumstances, they may properly be allocated to the periods affected.

While the accounting theory just quoted favours the allocation of income tax, it does so on the assumption that the allocation will have a significant effect on the reported income figure for the year. If not, the allocation should not be made because it merely introduces a complication and renders the interpretation of the financial statements that much more difficult for shareholders. An asset described as "Deferred charge for income tax", for example, is likely to have little meaning to the ordinary reader of a balance sheet.

The treatment referred to in the question appears to require the credit of a part of recorded revenue to a deferred revenue account each year, with a transfer back to current revenue in respect of deferred revenue of previous years for any balance of revenue which remains after payments under the warranty. To the extent that revenue is deferred, the related portion of income taxes payable would be charged to a deferred charge account instead of to a current income tax expense account; and to the extent that a transfer is made from deferred revenue account to current revenue in respect of the deferments of previous years, income tax expense reported for the current year would be increased and deferred charges for income taxes reduced. It is quite possible that the net effect of such an allocation of income tax would not be significant enough to justify the allocation.

An alternative accounting treatment would be not to defer revenue but to creat an "estimated liability for repair of products under warranty" by a charge against revenue. If the amount added to the estimated liability account were not allowed for income tax purposes, then presumably the actual payments under warranties would be allowed. Here again, the final effect may not be material enough to justify an allocation of income tax.

(*Comments and criticisms of the editor's reply are invited.*)

PROBLEMS AND SOLUTIONS

Solutions presented in this section are prepared by qualified accountants and reflect the personal views and opinions of the various contributors. They are designed not as models for submission to the examiner but rather as such discussion and explanation of the problem as will make its study of benefit to the student. Discussion of solutions presented is cordially invited.

PROBLEM 1

Primary Examination (Ontario), October 1955
Accounting I, Question 6 (15 marks)

On 1 Jan, 1954, White consigned 800 baskets of blueberries to Black, a commission merchant, to be sold by Black on account of White at the best obtainable prices at a 6 per cent commission on the sale price. White carried the blueberries in his merchandise stock at $6.00 per basket. White paid out the following charges on the shipment:

Packaging	$ 800.00
Freight	90.00
Insurance	46.00

Up to 15 Mar 1954 Black had paid storage expenses of $125.00 and cartage on sales of $75.00.

Black made the following sales:

February 3	400 baskets for $3,200.00
February 15	175 baskets for 1,550.00
March 3	160 baskets for 1,150.00

An account of sales was submitted by Black on 15 March along with one half of the gross proceeds. On 31 Mar, 1954, White's fiscal year end, Black reported that 35 baskets were unsaleable.

Required:

(a) Prepare journal entries to record the above information,
 (i) in the accounts of the consignee
 (ii) in the accounts of the consignor.

(b) What information should be included in an account sales submitted to a consignor?

A SOLUTION

(a)(i) Books of Black (Consignee)

1954			*Dr.*	*Cr.*
Mar. 15	White (consignor)		200.00	
	Bank			200.00
	Expenses re consignment:			
	Storage	$125.00		
	Cartage	75.00		
		$200.00		

		Dr.	Cr.
Feb. 3	Bank	3,200.00	
	Commissions earned		192.00
	White (consignor)		3,008.00
	Sale of 400 baskets on account of White		

Feb. 15	Bank	1,550.00	
	Commissions earned		93.00
	White (consignor)		1,457.00
	Sale of 175 baskets on account of White		
Mar. 3	Bank	1,150.00	
	Commissions earned		69.00
	White (consignor)		1,081.00
	Sale of 160 baskets on account of White		
Mar. 15	White (consignor)	2,950.00	
	Bank		2,950.00
	Remittance of one-half of gross proceeds to date		

(ii) BOOKS OF WHITE (CONSIGNOR)

1954		*Dr.*	*Cr.*
Jan. 1	Consignment inventory, Black	4,800.00	
	Merchandise stock		4,800.00
	Shipment of 800 baskets of blueberries on consignment		
Jan. 1	Consignment inventory, Black	936.00	
	Bank		936.00
	Charges in connection with consignment: Packaging $800.00 Freight 90.00 Insurance 46.00 $936.00		
Mar. 15	Bank	2,950.00	
	Account receivable, Black	2,396.00	
	Commission expense	354.00	
	Storage expense	125.00	
	Cartage	75.00	
	Sales revenue		5,900.00
	Account sales and remittance received from Black		
Mar. 31	Cost of goods sold	5,520.90	
	Consignment inventory, Black		5,520.90
	To record inventory of 30 baskets at $7.17 per basket, calculated as follows: Cost of 800 baskets $4,800.00 Packaging 800.00 Freight 90.00 Insurance 46.00 Laid-down cost $5,736.00 Unit cost $ 7.17 and to charge to Cost of goods sold 735 baskets sold and 35 baskets which are unsaleable		

(b) The following information should be included in an account sales submitted to a consignor:

1. Quantities of merchandise received from the consignor;
2. Quantities and dollar amounts of sales;
3. Quantities and condition of any merchandise remaining on hand;
4. Expenses paid by consignee on behalf of consignor;
5. Commissions on sales at agreed rates;
6. Cash collections and remittances to date;
7. Where goods have been sold on credit, the names of the debtors, balances owing, and terms of payment.

PROBLEM 2

Intermediate Examination, October 1956

Accounting I, Question 2 (12 marks)

R Co. Ltd. was incorporated under the Companies Act (Canada) on May 1, 1955, with authorized share capital as follows:

25,000 5% preference shares of a par value of $100 each, redeemable at 105,
20,000 common shares of no par value.

The following transactions affecting share capital occurred from the date of incorporation to May 15, 1956:

1955

May 1 12 common shares issued to the directors of the company at $25 each for cash.

May 2 5,000 preference shares offered for sale at $102.

May 15 3,000 common shares issued to promoters for organization expenses of $20,000 and for patents valued at $40,000.

June 30 Applications received for 5,500 preference shares with a deposit of $12 a share on application.

July 1 5,000 preference shares allotted and issued to subscribers with a request for the balance of cash owing on shares.

July 2 Refund made of deposits on applications not accepted.

July 15 Received all cash due, except for $180, on preference shares allotted and issued.

Aug. 31 10,000 preference shares sold to D Investment Dealers at $102.

Sept. 1 R Co. Ltd. acquired a controlling interest in E Co. Ltd. through the purchase of 10,000 common shares of E Co. Ltd. for $100,000. R Co. Ltd. paid $48,000 cash and issued 2,000 common shares for the balance.

1956

April 30 Directors resolve that an amount is to be set aside out of profits (which may be regarded as available) for the purpose of redeeming 5,000 preference shares.

May 15 5,000 preference shares redeemed for cash.

Required:

Journal entries, complete with narratives, to record the foregoing transactions.

A SOLUTION

R CO. LTD.

JOURNAL

1955

Date	Particulars	Dr.	Cr.
May 1	Cash	300	
	Capital stock issued – common		300
	To record issue of 12 common shares to directors at $25 per share, per minutes		
May 15	Organization expense	20,000	
	Patents	40,000	
	Capital stock issued – common		60,000
	Issue of 3,000 common shares in payment for organization expenses and patents acquired, per directors minutes		
June 30	Cash	66,000	
	Applicants – preference shares		66,000
	Application for 5,500 preference shares at $102 with deposit of $12 per share		
July 1	Applicants – preference shares	60,000	
	Subscribers – preference shares	450,000	
	Capital stock issued – preference shares		500,000
	Premium on preference shares		10,000
	Allotment and issue of 5,000 preference shares at $102 and final call of $90 per share, per directors minutes		
July 2	Applicants – preference shares	6,000	
	Cash		6,000
	Refund of deposit to unsuccessful applicants		
July 15	Cash	449,820	
	Subscribers – preference shares		449,820
	Receipt of cash on final call of $90 per share from holders of 4,998 preference shares		
Aug. 31	D Investment Dealers	1,020,000	
	Capital stock issued – preference shares		1,000,000
	Premium on preference shares		20,000
	Cash	1,020,000	
	D Investment Dealers		1,020,000
	Issue of 20,000 preference shares at $102 to D Investment Dealers, per directors minutes		

1956			
Sept. 1	Shares of E Co. Ltd.	100,000	
	Cash		48,000
	Capital stock issued – common		52,000
	Purchase of 10,000 common shares of S Co. Ltd. for cash, $48,000 and for 2,000 common shares issued at $26 each per directors minutes		
April 30	Earned surplus	515,000	
	Surplus appropriated for redemption of preference shares		515,000
	Amount set aside for redemption of 5,000 preference shares at $105 each per minutes: Total amount required – 5,000 @ $105 = $525,000 *Less* premium on issue – 5,000 @ $2.00 = 10,000 $515,000		
May 15	Capital stock issued – preference shares	500,000	
	Premium on preference shares	10,000	
	Loss on redemption of preference shares	15,000	
	Cash		525,000
	To record redemption of 5,000 preferred shares at 105 – originally issued at 102		
May 15	Surplus appropriated for redemption of preference shares	515,000	
	Capital surplus		500,000
	Loss on redemption of preference shares		15,000
	To transfer to capital surplus par value of preferred shares redeemed – 5,000 shares @ 100 = $500,000 and to write off the loss on redemption of preferred shares – 5,000 shares @ $3 = $ 15,000		

Examiner's Comments

Some candidates complicated their solutions unnecessarily by using too many accounts which merely "washed out".

PROBLEM 3

Final Examination, October 1956

Accounting I, Question 1 (18 marks)

You are the accountant for a new company which has been in operation for three months. You have set up the accounting system on a job-order cost basis and have established a 300% of direct labour cost factor to apply factory service.

The manager of the company has a working understanding of the cost system but knows little of accounting practice or procedure. He asks you the following questions:

(i) What general classes of expenses are not included in calculating factory service expense?

(ii) How did you arrive at the factory service rate of 300%?

(iii) Is the rate subject to change? If so, why and how often? If not, why not?

(iv) Does it matter if the rate is not correct?

(v) If the money actually spent on factory service is different from the amount absorbed by the rate, how does it show in the books? How does it show on the financial statements?

(vi) Is this amount written off at the year end? If so, to what account? If not, why not?

(vii) What is the main advantage of the direct labour cost basis of applying factory service?

(viii) Is the factory service rate applied to the labour cost of all employees in the plant? Why?

(ix) If we use one of our employees to install a new machine, do we charge his labour cost to the machine? Do we charge factory service on his labour to the machine? Why?

Required:

A brief outline of the points to be covered in your answer to each of the above questions.

A SOLUTION

(i) The general classes of expenses which are not included in factory service expense are those which are unrelated to production and operation of the factory, such as selling, administrative, and financial expenses. Labour costs which are directly related to production, and cost of raw materials used are also excluded from factory service expense.

(ii) The factory service rate of 300% was arrived at by taking an estimate of factory service costs incorporating both past experience and future plans, and dividing this amount by an estimate of the productive labour cost for the same period. The productive labour cost was, in turn, calculated by estimating the total factory labour cost and deducting the non-productive labour costs.

(iii) Yes, the rate is subject to change. It is essentially an estimate which should be corrected when one or more of the factors vary. If we find that we are consistently under or over absorbing the factory service, the present rate should be replaced with a new one based on more accurate or up-to-date estimates. Before making a change in the rate, however, one should ascertain that the discrepancy is not merely temporary, due perhaps to seasonal variations which will correct themselves over the year.

(iv) It does matter if the rate is not correct. The factory service is added to the cost of jobs in process and when a job is completed, it be-

comes part of its total cost. If the rate applied is unrealistic, the cost shown for completed jobs will not be a satisfactory basis for charging customers in special cases or, where the prices of the jobs are determined chiefly by competition with other firms, for measuring the profitability of the jobs.

(v) The estimated factory service charged to jobs is credited to "applied factory service" account. A comparison of this credit with the total of the various factory service accounts shows the correctness of the rate applied. The difference ("over-applied or under-applied factory service") is presented as a separate item on the statement showing cost of goods sold.

(vi) As a general rule the over-applied or under-applied factory service balance is closed to cost of goods sold account. If it is large, however, it may be necessary to prorate it between work in process inventory, finished goods inventory, and cost of goods sold.

(vii) The main advantage of the labour cost basis over the other methods is its simplicity. The required figures are available without supplementary computations.

(viii) The factory service rate is applied to the direct labour cost only, that is, to wages paid to employees who contribute directly to production. Under the job-order cost system, the labour cost which can be allocated directly to the specific jobs is charged to their cost. The other labour costs, called indirect labour costs, are charged to factory service accounts and distributed later at a specific rate.

(ix) In theory, factory service should normally be added to the cost of material and labour and the total cost of installation capitalized. The principle underlying this treatment is that the true cost of a machine is the total expenditure incurred to the moment when it is ready to work. In practice, however, this procedure is not always followed. It is generally accepted practice not to charge factory service to the cost of installing a machine unless the factory service was specifically incurred as a result of that installation. For example, if a foreman devotes all of his time to supervising the installation, the cost of his services should be capitalized. Other factory service costs which would be incurred regardless of the installation would not be charged to the cost of the machine.

Examiner's Comments

The examiner reports that some candidates did not confine their answers to a job order cost basis, and advanced points which applied to other systems such as a standard cost system.

PROBLEM 4

Final Examination, October 1956

Auditing I, Question 1 (18 marks)

What action, if any, should be taken by CA, the shareholders' auditor, to discharge his responsibility in each of the following unrelated situations? (*3 marks for each item*)

(i) A re-assessment is received from the Income Tax Department which involves a liability for a substantial amount of additional tax. The assessment was received one month after the fiscal year end of the company and for this reason the president considers that it should be disregarded in finalizing the accounts. He states that the company will appeal the assessment.

(ii) During the year, a company wrote off a sizeable account receivable on receipt of advice that the customer had been forced into bankruptcy by a secured creditor. A month after the company's fiscal year end, just before completing his report, the auditor learns from an outside source that unsecured creditors of the bankrupt company may receive as much as sixty percent of their claims.

(iii) The accounts receivable outstanding as at the company's fiscal year end consist of a few large balances. The president has instructed CA not to communicate directly with the debtors.

(iv) The year-end inventories of finished goods are based on book records. During the year physical checks have been made of various items, but no complete physical count has been made during the last three years.

(v) On counting the petty cash fund, CA finds that the vouchers and cash on hand exceed the established amount of the fund. CA also finds that an IOU from a former employee of the company who is now employed elsewhere is included among the petty cash vouchers.

(vi) On his first audit of the accounts of a closely held company, CA finds that the share records are not kept properly and that no one is able to provide an up-to-date listing of shareholders. Further investigation reveals that the minutes of directors' and shareholders' meetings have not been written up for two years.

A SOLUTION

(i) The shareholders' auditor should take the following action:

1. Determine the reason for the additional tax.
2. Consider the possibility of a successful appeal from the re-assessment.
3. Attempt to convince the president that the company's accounts and the financial statements presented to shareholders must disclose the re-assessment. If there is a reasonable chance of a successful appeal, a footnote to the balance sheet setting out the facts should suffice; if the success of an appeal appears doubtful, the additional liability should be included in the accounts.
4. Consider a qualification in his report to the shareholders, if unable to convince the president of the need for disclosure.

(ii) The auditor should take the following action:

1. Determine the status of the account in question by referring to correspondence on file, by discussion with officials of the client concern, and by communication with the trustee in bankruptcy.

2. If the recovery indicated seems certain, suggest that accounts receivable and bad debts expense be corrected in the accounts, or qualify his report to the shareholders if his recommendation is not followed (on the assumption that the amount involved in recovery is material in relation to the other items appearing in the financial statements).
3. If the recovery seems doubtful, suggest that no change be made in the financial statements.

(iii) The auditor should take the following action:

1. Explain to the president the advisability of a direct confirmation of the accounts.
2. If the president refuses to approve a direct confirmation, the auditor should qualify his report to the shareholders by referring to the limitation thus imposed upon the scope of his examination.
3. Verify the accounts receivable to the best of his ability from the accounting records of the company and by reference to subsequent remittances received from its customers.

(iv) The auditor should take the following action:

1. Qualify his report to the shareholders by referring to the lack of a complete physical inventory count if he has any doubt about the accuracy of the inventory records.
2. If his tests indicate that the stock records are being kept accurately and that no significant adjustments are being made when physical counts are taken of various items, and that over a period of time a sufficiently large portion of the inventory is checked by physical count, he need not qualify his report.

(v) The auditor should take the following action:

1. Ascertain when the petty cash fund was last counted.
2. Check to see whether cash receipts are being deposited intact, and inquire into the company's procedures for handling cash.
3. Determine the source of the excess funds which have been used to make the petty cash disbursements.
4. Discuss his findings with a responsible official of the client company and have the petty cash fund reimbursed to date and the excess cash deposited.
5. Recommend that the IOU amount be recorded as an account receivable and its collection followed up.

(vi) The auditor should take the following action:

1. Advise the company officials of the situation.
2. If directors' and shareholders' meetings have been held during the last two years, recommend that the company's solicitor bring the minutes and share records up to date. Inquire as to the important decisions which have been made at such meetings.
3. If no meetings have been held, recommend that in future they be held at least once a year.
4. Follow up the situation to see that it is corrected.

NEWS OF OUR MEMBERS

Alberta

James Kerr, M.B.E., C.A. has been appointed general manager of Calgary Brewing & Malting Co. Ltd.

Gordon F. McClary, C.A. announces the opening of an office for the practice of his profession at 203 Cowley Bldg., 9908-109th St., Edmonton.

Stewart W. Andrew, C.A. announces the opening of an office for the practice of his profession at 303 Insurance Exchange Bldg., 313 - 8th Ave. W., Calgary.

Clarkson, Gordon & Co. and Kinnaird, Aylen & Co., Chartered Accountants, announce the admission to partnership of A. Bruce Mitchell, C.A. Mr. Mitchell will be resident in Edmonton.

British Columbia

Maurice S. Richmond, C.A. and Murray Katzman, C.A. announce the formation of a partnership for the practice of their profession under the firm name of Richmond, Katzman & Co., Chartered Accountants, with offices at 810-12 Vancouver Block, 736 Granville St., Vancouver.

Bailey, Monteith, Holms & Co., Chartered Accountants, Scollard Bldg., Victoria, announce the admission to partnership of Gordon A. Green, C.A.

Irving G. Chertkow, C.A. announces the admission to partnership of Robert B. Liverant, B.A., C.A. Henceforth the practice of their profession will be carried on under the firm name of Irving G. Chertkow & Co., Chartered Accountants, with offices at 1220 Vancouver Block, Vancouver.

J. H. Provost, C.A. has been appointed a director and treasurer of Nelson & Harvey Ltd., Vancouver.

Dyke & Howard, Chartered Accountants, announce the removal of their offices to 1525 West 7th Ave., Vancouver.

Ontario

Chagnon & MacGillivray, Chartered Accountants, announce that Russel W. Lott, C.A. has been appointed resident partner of their Guelph office, located in the Toronto-Dominion Bank Bldg., Guelph.

Peters, Brown & Co., Chartered Accountants, announce the admission to partnership of William J. Detenbeck, C.A. and Robert W. Mann, C.A. Mr. Detenbeck is the resident partner of the Port Colborne office and Mr. Mann of the Fort Erie office.

W. E. Johnson & Co., Chartered Accountants, announce that henceforth the practice of their profession will be carried on under the firm name of Johnson, Stewart & Co., Chartered Accountants, with offices at 320 Bay St., Toronto.

W. Harold Rea, F.C.A., president of Canadian Oil Companies Ltd., Toronto, addressed the Saint John Board of Trade on Jan. 23, at the Admiral Beatty Hotel. He spoke about Russia where he spent 11 days as guest of the Soviet Petroleum Administration.

Albert O. Adamson, C.A. has been ordained to the Anglican clergy. Now 67 years of age, Mr. Adamson was formerly audit supervisor in the Auditor-General's office.

B. Eric Minns, C.A. has been appointed pension trust officer with The Canada Trust Co., Toronto.

R. G. Aman, C.A. has been appointed comptroller and assistant business manager of Winnipeg General Hospital.

Allan Pyzer, C.A. and R. Wilson Linton, C.A. announce the formation of a partnership for the practice of their profession under the firm name of Pyzer, Linton & Co., Chartered Accountants, with offices at 88 Richmond St. W., Toronto.

Herbert A. Watson, C.A. has been elected president of the Chamber of Commerce of Lindsay.

John F. Vaughan, C.A. has been appointed general manager of Port Weller Dry Docks Ltd., Port Weller.

Gerald L. Prefontaine, C.A. announces the opening of an office for the practice of his profession at 250 Besserer St., Ottawa.

Prince Edward Island

T. Earle Hickey, C.A. and C. C. Hickey, C.A. announce the formation of a partnership for the practice of their profession under the firm name of T. Earle Hickey & Co., Chartered Accountants, Summerside.

Quebec

George Berlind, C.A. announces the removal of his offices to Ste. 202, 187 Graham Blvd., Town of Mount Royal.

E. C. Leetham & Co., Chartered Accountants, 660 St. Catherine St. W., Montreal, announce the admission to partnership of Bertram C. Briand, C.A.

P. H. Greenwood, C.A. has been appointed general manager of the Conant Paints, Toronto.

Andre Mineau, C.A. has been appointed internal auditor of Canadian Marconi Co., Toronto.

Hugh M. Wallis, C.A. has been elected president of the Montreal Museum of Fine Arts.

P. S. Wise, C.A. has been elected president of the B'nai B'rith Hillel Foundation at McGill University.

Allan C. McColl, C.A. has been appointed assistant comptroller of Shawinigan Chemicals Ltd., Shawinigan Falls.

Allison B. Luke, C.A. of Como, Que. has been re-elected president of the Canadian Association of Nurserymen at the 34th annual convention held at London, Ont.

S. A. Doubilet & Co., Chartered Accountants, announce that henceforth they will conduct the practice of their profession under the firm name of Doubilet, Pinkus & Co., Chartered Accountants. They further announce the removal of their offices to Ste. 415, 5757 Decelles Ave., Montreal.

The editor welcomes information for this column. News of members and provincial Institutes' activities received up to and including the 13th of the month will appear in the following issue of the journal.

CHANGE OF ADDRESS

If you move you should advise your provincial Institute. If you want to receive prompt, uninterrupted service in the delivery of *The Canadian Chartered Accountant,* you can help by advising us also of your change of address. Your cooperation will be most helpful and greatly appreciated.

INSTITUTE NOTES

NEW BRUNSWICK INSTITUTE

C.A. certificates were presented to successful candidates in the 1956 final uniform examinations at a congratulatory dinner held by the New Brunswick Institute in Moncton on January 18. Gerald E. Martin was the guest speaker. Following the banquet, the Students' Society sponsored a dance at which the C.A.'s and their ladies were guests.

MANITOBA INSTITUTE

A. R. Hart, general manager of the Bank of Montreal, was guest speaker at a meeting on January 16 of the Institute of Chartered Accountants of Manitoba.

C.A. CLUB OF OTTAWA

Mr. J. R. M. Wilson was guest speaker at a luncheon meeting of the club on Thursday, January 17. He spoke on "Some Challenges Before Us".

C.A. CLUB OF WESTERN ONTARIO

The annual at home of the Chartered Accountants Club of Western Ontario took place on March 1 at the Hotel Arizona on Highway No. 4, south of Lambeth. Johnny Brennan's orchestra played.

NEWS FROM NORTHWEST ONTARIO

The Northwestern Ontario Chartered Accountants Association held a dinner meeting at the Port Arthur Country Club on Wednesday, January 29, 1957. At this meeting, the constitution of the association was formally approved.

A Chartered Accountants Student Association of Western Ontario has also been organized recently with the following executive: president, R. J. Geddes; vice-president, G. Garner; secretary-treasurer, E. R. Seal; directors, R. Scott and G. Silver. The main purpose of the association is to arrange for talks and discussions on variious accounting subjects of special interest to the students. The membership presently consists of 15 students at the Lakehead and 4 in the Kenora-Fort Frances area.

WINDSOR AND DISTRICT C.A. ASSOCIATION

A talk on the "Problems in Education" by Clare McLeod, Deputy Director of Education for the Windsor Board of Education, was the feature of the January dinner meeting of the Windsor and District Chartered Accountants Association. Prizes were presented to the following students in the district who had obtained the highest marks in the 1956 examinations: primary, E. A. Agnew; intermediate, R. O. Sorenson; final, W. G. Peters. Howard Wellington was chairman of the meeting.

ONTARIO INSTITUTE

University Recruitment Program — A subcommittee of the Public Relations Committee carried out an ambitious program at the University of Toronto this fall in an effort to interest non Commerce students in becoming chartered accountants. In November and December 8" x 6" advertisements were placed in seven issues of *The Varsity* dealing with the opportunities for careers in accounting. These were followed by personal letters to the men in the third and fourth years of the Faculty of Arts and meetings were arranged at each of the four Arts colleges. The meetings were intended to give interested students an opportunity to talk to chartered accountants who were also graduates of their college. The Institute's personnel selection test program was also offered for a nominal fee to university students. It is too early to judge the results although it is a fact that the meetings at the four colleges attracted only 17 students.

Lectures on Estate Planning — The Law Society of Upper Canada has offered practising members of the Institute the opportunity of subscribing to 25 tickets to attend the estate planning lectures to be held in Osgoode Hall on March 22, 23 and 29, 30. On Fridays there will be 5 lectures from 10:00 a.m. - 4:00 p.m. and a buffet luncheon. On Saturdays there will be 3 lectures from 10:00 a.m. to 1:00 p.m. The fee for the series is $15 per member. Applications with cheques payable to the Institute should be made in writing to the registrar. They will be accepted, one for each firm, in the order received. Other applications in excess of 25 will be placed on a waiting list in case of cancellations. Tickets and a detailed program will be sent as allotments are made.

Presentation of Certificates — 143 of the 176 new members by examination attended the convocation on February 8. Total attendance was 700, a new record for the occasion. Included in the group were J. G. Hrabovszky, a graduate of the University of Budapest; Henry Koren from Hamburg, Germany; and Bohomir Mateyko of Horodenka, Poland. W. M. Brace, F.C.A., addressed the graduates.

74th Anniversary Dinner — The ticket sale for the dinner to be held at 7:15 p.m. on Friday, March 8 will close at 2:00 p.m. the previous day.

Affiliation — Admitted to membership by affiliation on February 8, 1957 were G. E. Mitchelson (Inc. '55) D. W. Harris (Inc. '51) A. G. Barclay (Scot. '54) J. S. Dron (Eng. '54) and under by-law 4(c) P. N. Collinge (Natal '53).

ONTARIO STUDENTS NOTES

January Meeting — Walter L. Gordon, F.C.A., chairman of the Royal Commission on Canada's Economic Prospects, addressed the January meeting of the Association in Toronto. A capacity audience of 175 heard Mr. Gordon explain the work of the Commission and answer a number of questions concerning its findings. He was introduced by the president of the Association, Paul Higgins, and was thanked by the past president, Tracy Lloyd.

Molson Tour — 70 students, all who could be accommodated, enjoyed a conducted tour of the new Molson plant in Toronto on the evening of February 5. The brewery personnel looked after the party very well and refreshments were served at the conclusion of the tour. As it was not possible for everybody who wanted to take part to go on this first tour, a second date has been arranged for Wednesday, March 20, when another party will tour the plant. Members of the Association have already been advised of this second tour and the lists are now open.

QUEBEC INSTITUTE

Convocation — The annual presentation of prizes and certificates of the Quebec Institute will take place on the afternoon of Saturday, March 23 in the ballroom of the Ritz Carlton Hotel, Montreal. W. Givens Smith, president of the Canadian Institute, will address the successful candidates and their relatives and friends, and will present Canadian Institute silver medals to Ronald Edward Gallay of Montreal and Marc-Edouard Martel of Quebec City, who tied for the second highest standing in Canada in the final examination. These two were also joint winners of the Quebec Institute Gold Medal for the highest standing in the Province of Quebec.

Spring Conference — The first annual spring conference of the Quebec Institute will be held in conjunction with the annual meeting on Wednesday, June 12 at the University of Montreal on the northern slope of Mount Royal, Montreal. The conference will open at 9:00 a.m. and will include English, French and bilingual panel meetings and group discussions on a variety of subjects. Those attending the conference will be served luncheon at the University immediately following the annual meeting and election of officers. Chairman of the spring conference committee is Henri L. Belanger.

Annual Dinner The annual dinner of the Quebec Institute will be held at the Sheraton Mount Royal Hotel, Montreal, on the evening of Monday, June 12, following the spring conference.

The Society of Industrial and Cost Accountants in cooperation with The Montreal Board of Trade has extended an invitation to all members of the Institute to attend an executive seminar on "Appraisal of Electronic Business Applications". The one day conference, to be held in the Montreal Board of Trade building on April 18, 1957, will be designed for both the experienced executive who wants a refresher in fundamentals in addition to the latest developments, and the less experienced who wants a solid foundation of knowledge. Conducted under the direction of Ralph H. Eiden, Director of Electronic Applications, Management Service Division, Ernst & Ernst, Cleveland, Ohio, this conference will give participants the opportunity of hearing authoritative speakers in the field, taking part in stimulating floor discussions and exchanging ideas with executives from every branch of industry.

Since registrations for this meeting are limited to 175, members are urged to make plans now. Registration forms will be mailed to Quebec members approximately March 11. Additional information may be obtained from Miss C. Gougeon, Montreal Board of Trade, 300 St. Sacrement Street, Montreal.

QUEBEC STUDENTS SOCIETY

The Chartered Accountants Students Society of Quebec announces a dinner meeting to be held in the Spanish Room of the Queen's Hotel in Montreal, at 6.30 p.m. on Wednesday, March 27. The speaker will be Mr. Alan Chippindale, Director, Vice-President and Treasurer of Canadian Investment Funds Limited and Vice-President of Calvin Bullock Limited. His subject will be "Mutual Investment Funds".

The Society cordially invites all chartered accountants as well as all of its own members to attend and to take part in a question and answer period which will follow the speaker's remarks. Reservations are advisable and tickets may be obtained at the Institute's offices.

OBITUARIES

HAROLD ARTHUR SCARFF

The Institute of Chartered Accountants of Ontario announces with regret the sudden death of Harold Arthur Scarff of Windsor in his 57th year.

Mr. Scarff was the senior partner of Brokenshire, Scarff & Co. and auditor of the City of Windsor since 1937.

Born in Essex, Ontario, Mr. Scarff attended the University of Toronto after graduating from Essex High School. He was a student-in-accounts with A. S. Fitzgerald in Windsor and became a member in 1926. Only last year he was admitted a Fellow the Institute. He served on the senate of Assumption University.

To his wife and family the members of the Institute extend their sincere sympathy.

RICHARD W. OWENS

The Institute of Chartered Accountants of Quebec announces with deep regret the sudden death on December 16, 1956, of Richard W. Owens, a registered student of the Institute.

Mr. Owens, who was 29 years of age, was born and educated in Montreal and had been employed as a student-in-accounts with the firm of McDonald, Currie & Company since 1952. He was a member of the Executive Committee of the Chartered Accountants Students Society of Quebec.

The Council and members of the Institute and the Executive and members of the Students Society extend to the members of his family their most sincere sympathy.

CLASSIFIED ADVERTISEMENTS

Rates: ***Positions wanted, $7.00 per column inch; Positions offered, $10.00 per column inch; Open rate, $17.00 per column inch.***

All replies to box numbers should be sent to The Canadian Chartered Accountant, 69 Bloor Street East, Toronto 5, Ontario.

Closing date is 14th of preceding month

UNUSUAL OPPORTUNITY: One of Canada's large life insurance companies with head office in Toronto has openings for two chartered accountants in special work on a permanent basis. One position is in our advanced training department which deals with estate analysis, tax problems, business insurance and other advanced underwriting situations. A man with experience in these areas can assist us to increase the scope of this department and help to teach our managers and men the knowledge necessary to develop this type of underwriting. The other position is in our group annuity and pension department. We are planning on a broad development in this field and need a man with accounting background and business experience to specialize in group annuities and work out of our head office.

The men we want should have at least 5 years' experience after qualifying for their degree. Attractive salary, fringe benefits and permanent position with a real opportunity for advancement. Reply to Box 636 giving age, experience and salary requirement. All information treated confidentially.

CHARTERED ACCOUNTANT: Recent graduate required as audit supervisor by company in Toronto area. Excellent salary range and initial salary. As employer contact will be made only after initial interview, reply in strict confidence giving age, education, experience etc. to Box 637.

STUDENT WANTED by medium-sized Montreal firm of chartered accountants with a varied clientele and little out-of-town work. Age, educational status, and salary desired should be stated in application, which should be addressed to Box 635.

ASSISTANT COMPTROLLER WANTED: A large financial organization in New Brunswick requires a well-trained accountant, preferably a chartered accountant, to take over full responsibility for statement preparation, as well as all accounting and systems procedures and supervision.

The basic accounting system includes IBM electronic and punchcard equipment which will afford an opportunity for the right man to make full use of his personal initiative.

This is an opportunity for a career man to increase his training and responsibilities in an expanding position with commensurate income. Reply in confidence to Box 638.

COMPTROLLER: Group of insurance companies require a chartered accountant for the position of comptroller at the Canadian head office in Montreal. Applicant must be between the ages of thirty and thirty-five. Insurance experience not essential. Permanent position with excellent opportunities. All applications will be treated as confidential. Please submit full details of previous experience to Box 634.

CHARTERED ACCOUNTANT, B.Com., Jewish, age 29, desires responsible position with public firm offering prospect of eventual partnership arrangement. Box 629.

YOUNG CHARTERED ACCOUNTANT seeks position with public accounting firm in Toronto with prospect of eventual partnership or succession. Has small practice of his own. Box 640.

POSITION WANTED: Young, aggressive chartered accountant wishes to associate with Toronto public accountants with partnership or succession possibilities. Box 641.

PROFESSIONAL CARDS

MACLEOD, McDERMID, DIXON, BURNS, McCOLOUGH, LOVE & LEITCH

Barristers & Solicitors

6th Floor, Hollinsworth Building - - - Calgary, Alta.

PITBLADO, HOSKIN, GRUNDY, BENNEST & DRUMMOND-HAY.
PITBLADO, HOSKIN, McEWEN, ALSAKER, HUNTER & SWEATMAN

Barristers and Solicitors

Hamilton Building, 395 Main Street - - Winnipeg, Man.

STEWART, SMITH, MACKEEN, COVERT, ROGERS, SPERRY & COWAN

Barristers and Solicitors

Roy Building - - - - Halifax, N.S.

ROSS & ROBINSON

Barristers and Solicitors

Canadian Bank of Commerce Chambers - - Hamilton, Ont.

BORDEN, ELLIOT, KELLEY, PALMER & SANKEY

Barristers and Solicitors

25 King Street West - - - - Toronto 1, Ont.

ALAN DIGNAN, Q.C.

Barrister and Solicitor

Bloor Street & St. Clarens Avenue - - Toronto 4, Ont.

McLAUGHLIN, MACAULAY, MAY & SOWARD

Barristers and Solicitors

302 Bay Street - - - - Toronto 1, Ont.

OSLER, HOSKIN & HARCOURT

Barristers and Solicitors

The Dominion Bank Building, 68 Yonge Street - Toronto 1, Ont.

PLAXTON & COMPANY

Barristers and Solicitors

Suite 1207, 320 Bay Street - - - - Toronto 1, Ont.

WRIGHT & McTAGGART

Barristers and Solicitors

67 Yonge Street - - - - - Toronto 1, Ont.

BEAULIEU, BEAULIEU & CASGRAIN

Barristers and Solicitors

Kent Building, 10 St. James Street West - Montreal 1, Que.

DIXON, SENECAL, TURNBULL, MITCHELL, STAIRS, CULVER & KIERANS

Barristers and Solicitors

Bank of Canada Building - - Montreal 1, Que.

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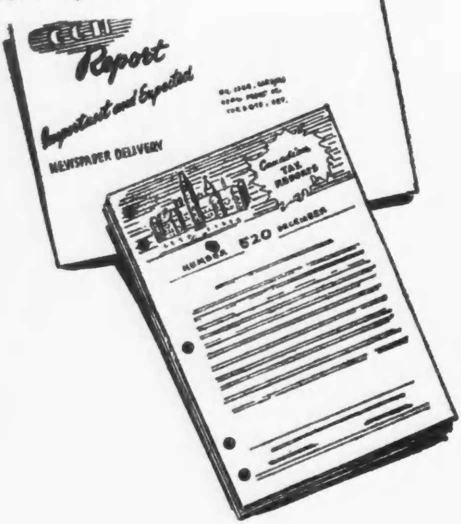

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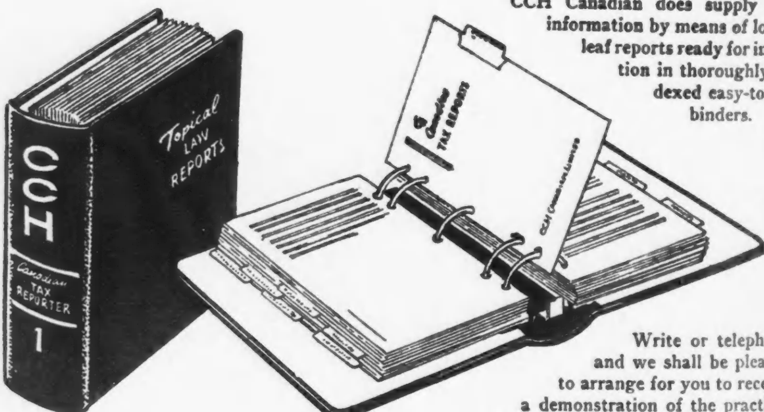

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